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REPORT

OF THE

COMMITTEE ON FORWARD MARKETS

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MINISTRY OF CIVIL SUPPLIES
GOVERNMENT OF INDIA
JUNE 1980

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APPOINTMENT OF THE COMMITTEE AND ITS TERMS OF REFERENCE

The Committee on Forward Markets was constituted by the Government of India in terms of Ministry of Commerce, Civil Supplies and Cooperation, (Department of Civil Supplies and Cooperation) Order No. 10(3)-IT/77 dated the 27th March, 1979 to :

(*i*) review the role that forward trading has played during the last 10 years ;

(*ii*) assess the role that forward trading can play in the prevailing economic conditions and marketing/distribution system in the commodities in which forward trading is possible, particularly in commodities in which resumption of forward trading is generally demanded ;

(*iii*) examine the extent to which forward trading in commodities in which such trading may be permitted could be of direct or indirect benefit to producers and consumers of the commodities ;

(*iv*) examine the extent to which forward trading has special role to play in promoting exports ;

(*v*) suggest measures to ensure that forward trading in the commodites in which it is allowed to be operative remains constructive and helps in maintaining prices within reasonable limits ;

(*vi*) suggest amendments to the Forward Contracts (Regulation) Act in the light of its recommendations particularly with a view to efficient enforcement of the Act to check illegal forward trading when such trading is prohibited under the Act ; and

(*vii*) suggest measures for strengthening the Forward Markets Commission to achieve the objective of making futures trading socially purposeful.

The Committee consisted of the following :

Dr. A.M. Khusro	Chairman
Dr. L.S. Venkataramanan	Member
Shri B.N. Kapre	Member
Dr. Vijay L. Kelkar	Member
Dr. P.N. Kaul	Member
Shri V.N. Lokur	Member
Shri M.G. Jawle	Member-Secretary

A copy of the order is at Annexure I.

2. The Committee was required to submit its report to the Government within a period of six months. The issues before the Committee being complex and needing a thorough and detailed examination, more time was required to complete its work. Moreover, many organisations and individuals interested in the subject were keen to give evidence before the Committee and the Committee had also to visit important centres of forward trading in the country. Hence, pursuant to the request of the Committee, the Government was good enough to grant extension of time till 30th June 1980 for the submission of its report.

Method of enquiry

(a) Issue of Questionnaire

3. In order to elicit detailed information on various matters relating to forward trading, particularly with reference to the terms of reference of the Committee, from the concerned interests, viz., recognised associations, registered associations, organisations and individuals with knowledge or experience of the subject and concerned authorities in the Central and State Governments, a detailed questionnaire was issued by the Committee. A copy of the questionnaire is given in Annexure II. The Committee issued a press note, on 27th April, 1979, requesting the concerned trade interests, organisations and members of the public to place their views and suggestions in the matter drawing their attention to the questionnaire framed for the purpose. In all, written replies were received from 76 associations including recognised and registered associations, 23 individuals and 10 Government authorities. A list of those from whom replies were received is given in Annexure III.

(b) Visits and meetings

4. The Committee held, in all, 16 meetings, out of which 8 were in Bombay in view of its importance as a commercial centre, terminal market and a prominent centre for futures trading. The Committee visited Delhi, Calcutta, Ahmedabad, Rajkot, Cochin and Trivandrum and held discussions with the concerned interests and studied the problems faced by the various functionaries in the marketing of the commodities with which they were concerned. In the process it obtained the views of diverse interests seeking the facility of futures trading as also some opposing it. The Committee sought the views of the concerned State Governments and also held discussions with the authorities of the Governments of Maharashtra, Gujarat, West Bengal and Kerala. The Committee's discussions with the Secretaries to the Departments of Commerce, Agriculture, Industry, Finance and Economic Affairs of the Government of India were also useful in the formulation of its views on various matters concerning the matter under study. A list of associations, firms and individuals whom the Committee met for discussions is given in Annexure IV.

Scheme of the report

5. Before we proceed with the report, we consider that it would be useful to give its broad pattern and salient features. We thought it necessary and useful to enunciate at the outset the Committee's approach to futures trading. This has been dealt with in Chapter 1 outlining the various attributes for futures trading and conditions under which futures trading can be economically feasible and socially desirable. In Chapter 2, an attempt has been made to explain in detail in as simple a manner as possible the theory and practice of futures trading. The subject of futures trading has been misunderstood by many and less understood by some with the result that it does not seem to have received the attention it deserves as an instrument to support the other existing market mechanisms. It is hoped that these Chapters would be useful to many of those who are interested in the subject of forward trading. The historical background of forward trading in India and the regulation of such trading have been dealt with in Chapter 3. The suitability of various commodities for futures trading under present conditions has been examined in Chapter 4 applying the criteria relevant to each commodity. The Committee has arrived at specific conclusions as to whether futures trading in a commodity should be permitted or not keeping in view the socio-economic conditions presently obtaining in the country and after consideration as to whether benefits from futures trading would accrue to producers and consumers in addition to traders. We have also examined the suitability and need for futures trading in some of the non-traditional commodities and made appropriate suggestions. The limited time at the disposal of the Committee did not permit it to make an in-depth study of these commodities as also various other commodities like potatoes, onions, apples, ginger, chillies, etc., in which there is scope for futures trading. The fulfilment of economic and technical requirements alone in a commodity is not enough for the satisfactory conduct of futures trading in it. There are a number of basic requisites for the conduct of such trading which are enumerated at some length in Chapter 5. Chapter 6 deals with non-transferable specific delivery (ntsd) contracts, their need and the steps to prevent the misuse of such contracts. In Chapter 7 we have proposed the amendments considered necessary to the Forward Contracts (Regulation) Act, 1952 to plug existing loopholes, for an efficient enforcement of the Act to check illegal forward trading and to vest additional powers in the Commission to secure speedy enforcement action. The recommendations made by the Committee would require an increase in the existing strength of the officers and the staff of the Forward Markets Commission. Suggestions in this regard have been made in Chapter 8. The final Chapter 9 gives a summary of the conclusions and recommendations of the Committee.

Acknowledgements

6. We take this opportunity of thanking the representatives of various bodies as also the many individuals who gave valuable evidence before us; we also wish to record our appreciation of the organisations and persons who were good enough to send us written memoranda, statistics and other information in response to our questionnaire.

7. The Committee had the special advantage of having as its members, Shri B. N. Kapre and Shri M.G. Jawle, Chairman and Member respectively of the Forward Markets Commission. The Committee benefitted greatly from their expertise and experience in this complicated area. We are specially indebted to Shri M.G. Jawle, our Member-Secretary, for his technical and organisational assistance of a high order. The Report has gained from his wide knowledge of the theory, working and regulation of forward markets.

8. The Committee would also like to place on record its high appreciation of very able assistance rendered to it by the officers of the Forward Markets Commission, Shri S.S.Pradhan, Director, Smt. S.M. Rege, Deputy Director, Shri A.T. Koshy, Inspecting Officer and Smt. S.R. Singh Research Officer, in the preparation of this Report. Their expert knowledge of the subjec made our deliberations more meaningful and our work relatively easy. The Committee would also like to thank Smt. S.S. Karkhanis and Shri M. Hemantha, Senior Research Assistants and Shri R.S. Nair, Reporter, and other staff of the Commission for all the necessary secretarial assistance and the excellent arrangements at meetings which made the expeditious disposal of the work possible.

CHAPTER 1

APPROACH TO FUTURES TRADING

Futures trading is a very sophisticated mechanism which assists in the marketing of commodities. Its principal function is to enable the trading interests to shift the risk involved in such activities, arising out of the adverse price fluctuations, to those who are willing to assume it in the hope of making some profit. The other benefits attributed to futures trading are that it lowers the marketing cost by reducing the risk involved in marketing, serves as a barometer of the future trend of prices and helps stabilisation of prices by restricting the steep fall or sharp rise in them during the peak or lean periods of the season. There is, however, a lot of misconception in the public mind about the beneficial effects of futures trading partly due to lack of understanding of its functions and partly due to possible dangers of speculation associated with it. We have, in Chapter 2, explained with as little use of technical jargon as possible, the basic theoretical and practical aspects of the working of a futures market. In this Chapter we have outlined our basic approach towards futures trading.

Conditions for the fitness of a commodity for futures trading

2. Not all commodities are fit for being traded in the futures markets.[1] To be capable of being traded in the futures market a commodity should be *homogeneous,* meaning that the units of the commodity should be interchangeable. So long as a bale of cotton is defined as being of the same grade, it does not matter to the buyer whether he gets one set of 100 bales or another. When wheat of a certain defined category is stored together in the same godown, it does not matter which tonne of wheat one takes in any transaction.

3. The second attribute for futures trading is that a commodity should be *capable of being standardised in one or more grades.* Futures contracts do not mention particular grades and qualities but are executed in terms of a pre-defined standard grade so that other grades of the same commodity can be separated by a pre-defined premium or discount on the price contracted for the standard grade.

4. It is yet another important characteristic for a commodity's capability for futures trading that its *supply and demand should be large* so that speculators with large financial resources are not able to obtain control of a substantial portion of it. The futures market for the commodity, in other words, should be so large that the largest of speculators constitutes but a small fraction of the market in terms of the biggest purchase or sale he can effect.

5. To be eligible for futures trading a commodity must necessarily be relatively *free from substantial control* either by a Governmental or public authority or a private organisation, cartel, association, corporation or individual. This means that in general the commodity should be able to flow to the markets freely and unhampered by interventions and restraints. Whenever for social or economic reasons a Government finds it necessary to ration, limit, or regulate the demand for a commodity, or fixes a support price or procurement price and follows it up by a procurement operation or delivery quotas and a net-work of ration shops or distribution points selling limited quantities at fixed prices, the eligibility of a commodity for futures trading is destroyed. This is the reason why, even though grains like rice, wheat, corn and maize are traded in several countries of the world on the futures markets, we cannot advocate a similar policy in this country, inasmuch as the important social requirement of providing grain in a guaranteed manner to low income consumers at a low price makes it necessary for Indian Government to operate a public distribution system in major foodgrains and makes it much less important, in fact unnecessary, to operate futures markets in grains.

6. It is also a necessity for a commodity's eligibility for futures trading that its *supply and/or demand must be uncertain.* When both supply and demand are certain, prices get readily adjusted without the intervention of an organised market. When a commodity is subject to season-to-season and year-to-year variations in supply and demand, the problem of oscillation in prices, often resulting in high peaks and low valleys and the consequences of such peaks and valleys for consumers and producers, must engage the attention of the economic and social analyst. Either the Government should then intervene with a full fledged mechanism like price control and public distribution system (if the commodity is of obvious social significance) or instruments like forward trading would have to be invoked, provided these instruments dampen the peaks and lift up the valleys.

7. Another obvious pre-requisite of a commodity for futures trading is that it *should not be perishable nor subject to changes in style and fashions,* as is the case, say, with shoes. As a futures contract requires delivery several months in the future, perishable and fashionable commodities do not meet the requirements of futures trading.

8. Lastly, even when a commodity has fulfilled all these conditions, the organisation of futures trading in the commodity requires that the leading segments of the production and trade sectors are active participants in it to supply adequate quantity of hedging contracts. This along with the operations of speculators, who come forward to assume the risk which hedgers desire

[1]For details, see Commodity Exchanges and Futures Trading by Baer and Saxon—Pages 110—125.

to shift, should be large enough to make the market broad and liquid, In the absence of production and trade segments, only speculators would remain in the futures market and that would not be a healthy circumstance for futures trading.

9. These considerations no doubt limit the possibility of futures trading to a relatively small number of commodities which fulfil all the aforementioned requirements. However, it must be stated that, in practice, many commodities in which futures trading is conducted may not fully satisfy all these requirements. For instance, in some of the commodities, the process of standardisation and grading has been quickened by the introduction of futures trading in them. Also, some participation or intervention by the State in the marketing of a commodity has been there since early thirties in many important commodities but this has not come in the way of practising futures trading in them. Again, the development of cold storage and other technological advancements for preserving commodities have taken away the limitation arising on account of perishability and at present futures trading in many foreign countries is conducted even in commodities like eggs, butter, potatoes, onions, concentrated orange juice, etc.

Enlargement of future volume of demand and supply may favour futures trading in India

10. It is a necessary condition for a successful operation of futures markets that the volume of demand and supply of the commodity to be traded in the futures should be large. In past years, partly owing to poverty and partly due to the predominance of foodgrains in agricultural production (only about 40 per cent of foodgrains production is marketed), the volume of demands and supplies for most agricultural commodities was relatively small. However, as time goes by, the demand for foodgrains does not increase in the same proportion as population or income. For a few more years to come, while the foodgrains demands in the upper income brackets of the Indian population will increase much more slowly, compared to population growth, the foodgrains demands among the bottom 3 or 4 poorest income deciles of population will continue to grow as fast as population growth, as the current levels of nutrition and food intake are very low. Once this trend is over, it is a certainty that the rate of increase of foodgrains demands will be less than the rate of population increase. On the other hand, the demand for agricultural commodities other than cereals and pulses are bound to increase with an increase in the level of national income and population. In particular, groundnuts, other edible and non-edible oilseeds and all the industrial raw materials produced in the agricultural sector, are likely to show a rapid growth of demand. In recent times while the major cereals, in particular, wheat and cotton have undergone a substantial technological change, other foodgrains, especially the inferior foodgrains, and almost all industrial raw materials produced in agriculture have been stagnating owing to a lack of technological breakthrough. As more resources are bound to be concentrated in these commodities, supplies are most likely to respond to growth in demands, and the markets for almost all agricultural commodities, except cereals, and in particular inferior cereals, are bound to grow. As it is a necessary condition for a satisfactory operation of futures markets that supply and demand should be large, Indian conditions are most likely to become more and more favourable for forward trading in these commodities as a result of the expansion of the volumes of demands and supplies.

11. It should also be noted that in the case of foodgrains the market in which demand meets market arrivals, is confined only to a certain proportion of the produce, say 40 per cent. The other 60 per cent or so is retained by the growers themselves for their own consumption. In the case of other agricultural commodities the case is entirely different and in most items almost the whole of production is for marketing. The future expansion of volume is, therefore, going to be more rapid in those commodities which are marketed almost wholly and such an expansion will naturally lend itself better to futures trading which requires a larger rather than smaller volume for effective functioning. The expansion of the market size generally goes with the improvement in market sophistications and this too is a favourable circumstance for the operation of futures markets.

The impossibility of extending the Price Control and Public Distribution mechanism to any but the most crucial commodities, may favour futures trading in Serial commodities other than major foodgrains

12. It is well known that in a relatively poor country like India, the basic and compulsive foodgrains requirements of the very large population with low incomes compels the government to intervene in the foodgrains markets and regulate foodgrains distribution through various devices. Thus in rice and wheat and some other foodgrains, there is a complex system of regulation and control involving the fixing of support prices, the procurement of grain, the provision of a large storage capacity, the operation, quite often, of a rationing mechanism and a vast net-work of public distribution agencies. This social necessity involves the Government in a complex and costly distributive apparatus which ties up a great deal of Governmental resources. It also involves the Government in a huge amount of subsidy currently amounting to perhaps Rs. 600 crores or so on foodgrains account alone. Now, this machinery, expensive as it is, is likely to remain confined only to major necessities and cannot be repeated for commodities other than the most urgent ones. That this mechanism of regulation and control can be multiplied in the case of half a dozen or a dozen other commodities is not on the cards as the costs are bound to be prohibitive.

13. Once the application of the current mechanism of regulation, price control and distribution control to most other agricultural commodities is ruled out, the question arises as to what other methods would be used to regulate the prices of these other commodities. And many of these commodities are such that they exhibit a high degree of price fluctuations as in the case of pulses, groundnuts, other oilseeds, etc. A

restraint somehow on their price fluctuations is necessary as much dislocation is caused by the erratic upward and downward price movements. It is in this context of the impossibility of a complex control and distribution mechanism in most agricultural commodities that futures trading as a possible measure, in suitable cases, for dampening the peaks and lifting up the valleys of prices is to be considered and in some cases it may turn out to be a necessity.

Forward trading cannot be recommended unless the gains to traders can be shown to be accompanied by gains to producers, manufactures and consumers. Social gain and not private gain is the justification for forward trading and this can be established only in some cases

14. If the gains from futures trading accrued only to those who traded in the futures market and to nobody else, or indeed, if the gains to futures traders were accompanied by losses to producers, manufacturers, consumers and other social interests, this Committee would not recommend resort to futures trading at all. It is a condition for what is called Pareto—optimality that some members of the society should gain from a given policy while nobody should lose. If it can be demonstrated that as a result of futures trading the gains to traders co-exist with gains to growers, manufacturers and consumers, then a clear case for futures trading can be said to exist. This Committee is, therefore, very keen to analyse and establish whether or not—and under what conditions and in what commodities—the gains to traders accrue alongside gains to growers, manufacturers and consumers. It seems from our analysis in this report that only in some cases such all round gains through futures trading are possible. This rests primarily on three factors as follows :—

(i) When futures trading is not permitted (in the commodities which fulfil all the aforementioned conditions and attributes for futures trading) only spot trading, or what is called ready market or trading for delivery on forward basis exists. In such cases a genuine trader or manufacturer who wants to buy the commodity for a genuine physical need has no guarantee that the price of the commodity he has bought will not decline seriously in the future; nor, if he has sold the commodity, is there a guarantee that prices would not increase sharply by the time he comes to procure and deliver the commodity. Even if the price fall or rise is small, the losses can be large if the transaction involves a large volume of sales and purchases in the spot market. There has to be a system of insuring against such losses. In the absence of any insurance cover to eliminate the risk of such losses the buyer or seller will not undertake the transaction at all, so that genuine physical needs of manufacturing, consuming, etc. will be hampered seriously, or, if the transaction is undertaken, there will be a great deal of riskiness attached to it. We note that in the absence of a risk-covering machinery one is left with nothing but speculation. A genuine trader or manufacturer who buys for a genuine physical requirement has necessarily to speculate and thus turns a speculator per force. In the absence of forward trading speculation is all that remains.

(ii) In a genuine futures market, speculation no doubt is an element of the aggregate transactions, but often only one element amongst many. There are in the futures markets many speculators who are neither manufacturers nor traders nor producers nor consumers—and one may object to their presence. Nevertheless, they serve to enlarge the volume of transactions and introduce a competitive element which takes a view of the market contrary to other views. For instance, when many a manufacturer or trader is taking a view that prices are going to rise, thus tending, in fact, to push up prices, some operators will take a contrary view to the effect that prices are going to fall. On the other hand, when traders and manufacturers generally believe that prices are likely to decline in the future, some operators may take the view that prices will rise. It is precisely the presence of such contrary views of the future by some operators in the market that brings sobriety in the market and prevents prices in the futures markets from rising too much or falling too sharply. And to the extent the futures prices do exert an influence on the spot prices, as they often do, the fluctuations in the spot market prices are also constrained. The futures markets along with their hedging operations thus become a force in reducing price oscillations and bringing in a more stable situation.

(iii) We also note that trading in the futures market is not undertaken only by speculators. There are several motives with which the members of the market (buyers and sellers) operate in the futures. First there is a speculator, though not necessarily the predominant element in the market. There is then the producer or the trader who has to keep adequate stocks of a commodity in order to meet a call for more deliveries by the manufacturers and consumers. Having produced (if they are producers) or bought in the ready (if they are traders), these persons must cover their risk and would, therefore, have to hedge against possible loss through a futures sales contract. There is then the manufacturer who has bought the raw material to embody it in due course in manufactured goods. He too must make sure that a possible loss owing to a fall in price is adequately covered by a hedging activity and a sales contract in the futures market. There is then the exporter or importer who operates with similar motives and must hedge against the risk of loss.

In suitable cases, futures trading will decrease risk and reduce the price spread

15. If futures trading (in the relevant commodities which fulfil the requirements) did not exist, many genuine transactions would never be undertaken and the size of the spot market would itself shrink; or, if the spot buying and selling was resorted to, riskiness all round would increase.

16. In that case, that is in the absence of futures market in appropriate commodities, the traders and manufacturers would attempt to cover their risks by attempting to charge a higher price to the consumers or to pay a lower price to the producers. In other words, the margin between what the producer receives and what the consumer pays would be widened just because no adequate method of covering the risk of traders and manufacturers was provided. It is obvious that in the absence of future trading and risk minimisations, as the producer (farmer) would get less, his motivation to produce more and, indeed, his investment capability (which depends upon higher receipts, among other things) would be reduced. On the other side, in the absence of futures trading, as the consumer pays more, demands may get constrained (as demand is generally less at a higher price) and the final retail market would not be widened as it would be when, in appropriate cases, futures trading exists. It is clear that futures trading, in appropriate cases and suitable conditions, makes the return to the producers higher and the price to the consumers lower. In effect it reduces what is called the *price spread.*

In suitable cases, futures trading will reduce price fluctuations and could have wholesome effects on production, trade and manufacturing

17. Not only does futures trading in genuine cases reduce the price spread, there are strong reasons for believing that it also reduces price fluctuations. Here we distinguish three different cases :—

Case 1—Where there is no clear upward or downward trend in prices but prices fluctuate over the seasons and over the years, around an approximately constant average level;

Case 2—Where there is an upward price trend and prices fluctuate over the seasons and years around the rising trend;

Case 3—Where there is a downward price trend and prices fluctuate over the seasons and years around the declining trend.

18. In the first case of fluctuations around a constant average level, it is obvious that with the approach of the harvest season every one expects a price trough but opinions differ about how deep the trough will be, as no one generally has full and final information. Similarly in the off-season every one expects the prices to rise but some expect a higher price peak than others. There are also differences of opinion as to when exactly the peak and the trough will occur. Also between one year and next there are differences of opinion about what the coming year has in store. It is precisely the existence of these differences in opinion that creates in the futures markets some buyers when the rest of the members are expecting a price fall, and some sellers when the rest are anticipating a price rise. It is this contrary view which creates some buyers when many want to sell and some sellers when many want to buy. These contrary opinions, and the buying and selling actions on their part, reduce price fluctuations in the futures markets. And to the extent this market influences the spot market, fluctuations in the spot market are also reduced. In this case, at any rate, futures markets do have a sobering influence and minimise price fluctuations with consequent healthy effects on producers, manufacturers as well as consumers.

In some cases futures trading may not be beneficial in short periods but will nevertheless remain a long term answer in terms of enlarged futures markets

19. The second case of a clearly established and discernible upward trend with seasonal and other fluctuations super-imposed thereon, can be a matter of some controversy. In such circumstances when everyone is expecting a price rise, both trendwise and seasonally, it may be thought that there are no dissenting opinions. All opinions would seem to converge over a price rise. It is thought that under these circumstances if speculators entered the futures market they would also be buyers rather than sellers and their buying activity may further aggravate the price rise. The futures prices will then stand above the spot prices and would be rising over time. This, it is thought, will be a compelling force for further inflation of the commodity price and there will be no saving factors leading to a downturn of price. Thus an important body of opinion, in particular official opinion, stands in favour of banning futures markets under these circumstances.

20. This opinion appears to have a good deal of weight and cannot be dismissed lightly. But then there are two types of sub-cases in this major case, which need to be clearly understood. One sub-case is that, even when the overall price trend is upward, the seasonal troughs are also sizeable so that there could be a divergence of views amongst the operators with regard to the point of time when the trough would be reached and with regard to its level. The second sub-case is that not only the overall price trend is upwards, but the post-harvest lows are also very nominal so that there is a general convergence of views that the price trend would soon be upwards. In the first sub-case, futures trading has a role to play inasmuch as the divergence of views with regard to the time when the trough would be reached and with regard to its level could be fully exploited and the market got stabilised. In regard to the second sub-case, it would appear that, the general convergence of opinion being for an early resumption of the uptrend, when futures market is a narrow market with a relatively few operators, it is possible there are few or no dissenting opinions. In such a situation when buyers buy, they do so at a much higher price since the sellers are also expecting a higher price. In that case inflation can be aggravated. But it should be noted that the answer can also lie in having a larger rather than a smaller futures market so that dissenting opinion is also held by a fairly large number of operators. Banning futures

market at the slightest of inflationary provocation every now and then, restricts the size of the futures market and prevents it from growing into a large, competitive, diversified and resilient market. It can be conceded, however, that during patently inflationary situations both trend-wise and seasonally, of the second type, a narrow futures market provides a case for stopping futures trading at any rate for short periods. From a longer-time stand point, however, the enlargement of the futures market is the right answer to an inflationary situation.

21. The third case of a downward price trend with seasonal and other fluctuations superimposed is just the reverse of the second case. Here, too, if futures markets were narrow and all opinions converged towards a declining price expectation, prices would tumble rapidly as everyone would want to sell. However, we note again that where there are sellers, there must also be some buyers in order that sellers sell. Here, from a short period narrow stand point, the answer would seem to be a ban on futures trading. But here, too, the long-term and sensible solution lies in the enlargement of the futures market so that when numerous operators are behaving (selling) as though prices would fall a large number of dissenting buyers exists who counter the downward price tendency and vice versa.

22. In this case, however, one important saving factor should be noticed. Selling pressure exists generally when supplies and stocks are abundant compared to demand. As surplus supplies and a surfeit of stocks use up the existing storage capacity, a normal tendency emerges to reduce stocks as stocking is expensive. This brings into being, and increases, the tendency to reduce stocks and to sell more aggressively the finished commodities in which primary commodities are embodied. This, in due course, creates circumstances which lead to more buying and ends the era of downward price trends and fluctuations. It would, therefore, perhaps be quite wrong to ban the futures markets in these circumstances at every provocation. It would be better to continue the market and allow it to keep on expanding so that adequate dissenting opinion emerges.

23. Our conclusion on these basis would be that in the relevant commodities generally considered suitable for futures trading on the basis of the criteria mentioned earlier, futures markets should be allowed to operate when there is no secular upward or downward trend in prices but only seasonal and other fluctuations exist. (This matter has been taken up commodity-wise for detailed investigation in a subsequent chapter). This is a good set of circumstances for futures trading. In the other two cases of inflationary and deflationary trends with fluctuations superimposed, the short period recommendations can be to stop the futures markets, particularly in persistent inflationary times. But from a long period consideration of enlarging the competitive resilience and dissenting opinion in the futures market, it would not be a disadvantage to the country if futures market in the appropriate commodities were to continue. But let it be understood that before advocating the opening or the confirmation of futures markets we should like to apply in a forthcoming chapter the criteria developed earlier, examine each commodity in some detail, in order to study the nature of its market and its social importance (requiring or not requiring other forms of price and distribution controls) and to establish whether forward contracts will merely benefit the traders or will provide gains to society as a whole—inclusive of producers, manufacturers and consumers.

24. Theoretical analysis suggest, as indicated elsewhere, that if futures markets did not exist in appropriate commodities the buyers and sellers in the ready market, including those who require the commodity for genuine trading and manufacturing purposes, would be obliged to hold undue stocks or forced not to undertake many a genuine and necessary transaction. They will also be forced to speculate. In the absence of futures trading, speculation will become a very large part of the ready activity, even of genuine traders and manufacturers. Futures markets, by providing hedge facilities enable the operators to cover the risk of the losses and thus reduce the spread between the prices received by the producers and the prices paid by consumers. In the absence of hedging and risk minimisation afforded by the futures market, the consumer price will be higher and the producer price will be lower. Both will work to the detriment of consumers and producers.

25. Because of the existence of dissenting opinion in a large and competitive futures market, futures prices generally tend to stand above the spot prices when spot prices are low or falling. This acts as a corrective upward influence on the spot prices. Conversely the futures prices generally tend to be lower than the spot prices when the spot prices are high or rising. This too exerts a sobering downward influence on the spot prices. Thus, with futures trading, the spot or the ready market will be a scene of small, less violent and less frequent fluctuations than it would be if futures markets were not permitted.

Futures markets become useful and resilient when producers and manufacturers begin to participate and benefit, alongside traders and speculators

26. Once it is seen that the existence of a healthy futures market in suitable commodities narrows down the price spread as well as the price fluctuations, it becomes clear that producers will stand to benefit from the existence of a futures market. In fact it is when the producers and the manufacturers, as well as the traders and the speculators, begin to become operators in the futures market, that the market takes a healthy and competitive shape and fulfils the destiny of a good market organisation.

In the absence of large open forward markets, monopoly/monopsony or oligopoly/oligopsony situations arise and black dealings grow

27. It has been noticed by this Committee that even when futures markets are banned, people continue to indulge in futures trading on the sly. Questionable deals are struck which are subject to no professional control or genuine arbitration. These deals are the

generators of undeclared black incomes and a cause of much social loss. In any event the number of operators in the surreptitious and illegal futures trading operations is very small, by definition. The smallness of such illegal markets enables a few large operators to corner the markets. Competition is eliminated and monopolistic or oligopolistic situations (one or a few sellers) and monopsonistic or oligopsonistic conditions (one or a few buyers) begin to characterise the markets. It is precisely these situations that should be guarded against.

Law and order machinery is not able to tackle the situation effectively

28. We have further noted that the law and order machinery is never able to lay its hands upon and bring to book all or even a substantial proportion of illegal operators. On top of it, all dealings in illegal markets often use and generate black earnings, and cause a further social loss as black earnings are neither conducive to economic growth nor to a more equitable distribution of income and wealth. No Government or other authority interested in growth and egalitarian income distribution can remain a spectator of such illegal and antisocial situations. It is, therefore, far better to enlarge the fold of legal forward transactions by encouraging genuine transactions and giving incentives to producers, manufacturers, traders and other users of commodities to participate in legitimate futures markets.

29. What is said above about illegal futures transactions also applies to forward contracts other than futures contracts—i.e. transferable specific delivery (tsd) and non-transferable specific delivery (ntsd) contracts when these are not permitted. Illegal futures trading is secretive and bilateral in character while genuine futures transactions are undertaken in the hall of the exchange under the guidance of a well established association and are known to all brokers. It is far better to promote healthy and open transactions than secret and bilateral ones.

30. In a forthcoming Chapter (Chapter 4) we propose to apply the criteria for socially justifiable futures trading developed in the present Chapter to a number of commodities and deduce conclusions as to whether futures trading should or should not be allowed in those commodities.

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CHAPTER 2

THEORY AND PRACTICE OF FUTURES TRADING

Futures contracts and other forward contracts

Futures trading has been defined by Prof. Holbrook Working as "trading conducted under special regulations and conventions, more restrictive than those applied to any other class of commodity transactions, which serves primarily to facilitate hedging and speculation by promoting exceptional convenience and economy of the transactions".[1]

2. It is necessary to distinguish between futures or hedge contract and other types of forward contracts. In any society which has to make arrangements for a continuous supply of a commodity, trading activity cannot be confined to the immediate present needs. A manufacturer or processor has to ensure in advance that he would get his supplies of raw material at the appropriate time and this he may do by entering into a purchase contract with a trader. The trader may, in turn, enter into a similar contract with a producer much in advance of the actual production or harvesting of the commodity. These 'forward contracts', sometimes also called 'time contracts',[2] are contracts for giving and taking actual delivery of goods at a specified price and at a specified future date. The use of these contracts has preceded the development of futures trading.

3. When 'forward contracts' of the types described above became a part of the normal marketing process, the development of what are called 'futures' or 'hedge' contracts became an economic necessity, provided the commodities concerned had the requisite characteristics to facilitate such trading in them smoothly. The futures contract was evolved to enable the various functionaries, engaged in merchandising a commodity or its processed products, such as dealers, stockists, commission agents, processors, etc., to hedge i.e. to protect themselves against the risk of unpredictable price fluctuations over time in the commodity. All these functionaries, dealing in the commodity have to store and carry forward stocks of the commodity either in its raw or processed form over time in the course of which they are exposed to the possibility of unforeseen price fluctuations, which may cause them huge losses.

Need to carry stocks

4. Stocks of many commodities need to be carried forward over time, for various reasons. First, certain commodities take shape of final consumers' goods only after lengthy manufacturing processes. Secondly, certain commodities, particularly agricultural commodities, cannot be produced continuously and have to be stocked because the total supply cannot be consumed immediately. Thirdly, the supply of such discontinuously produced commodities cannot be precisely adjusted to demand, being generally governed by natural conditions beyond human control, such as rains, general weather conditions, etc., and these commodities have to be stocked to meet future uncertainties. Fourthly even the commodities that can be continuously produced, have to be stocked because it is not economical to vary the rate of output in accordance with uncertain variations in demand.

Need for a method to protect stockists from price fluctuations

5. One who has to stock commodities in the course of his genuine business, exposes himself to risks arising out of possible fluctuations in prices of the commodities stocked. The fluctuations in prices may favour him or may affect him adversely. In other words, the risk of price fluctuation is speculative in nature. If the price fluctuations favour him, his business profit would cover not only his costs and remuneration for his services and entrepreneurship but also speculative profits due to changes in the prices. If the fluctuations move against him, the loss due to such unfavourable fluctuations may even wipe out his genuinely earned profit. Many businessmen dealing in commodities, therefore, desire to segregate the speculative element from their business by passing it on to others who are willing to shoulder it in the hope of making a profit. This segregation is achieved by 'hedging operations' in a futures market. A futures market, contrary to the popular belief, is not a market for speculative trading only. One of its principal functions is to offer facility to dealers and manufacturers to segregate speculation from their business by resorting to hedging. In the absence of hedging, speculative activity becomes a part of trading in actual commodity itself.

Main characteristics of futures trading

6. The main characteristics which distinguish futures trading from the other types of trading, are as follows. First, futures trading is necessarily organised under the auspices of a market association so that such trading is confined to or conducted through members of the association in accordance with the procedure laid down in the rules and bye-laws of the association. Secondly, the terms of the futures contracts to be traded in are highly standardised in respect of grade or quality of the commodity, quantity, i.e. unit of trading, place and time of delivery, etc.

Standardisation

7. Futures contracts are framed in such a way as to secure a high degree of perfection and liquidity in

[1] Futures Trading and Hedging—American Economic Review—Vol. XXIII 1953.

[2] In the Forward Contracts (Regulation) Act, 1952, these types of forward or time contracts are called non-transferable specific delivery (ntsd) contracts.

the market by means of completely standardising their terms. The noteworthy features of this standardisation are as follows. The contract is entered into for a fixed variety called 'basis' variety or grade selected for the purpose, taking into account its supply and the representative character with reference to other grades of the commodity. It is usually the one which is in the widest commercial use. The seller has the option to deliver against the contract either the 'basis' grade or other prescribed alternate grades known as 'tenderable grades'. These alternate grades may be superior or inferior to the 'basis' grade and are, therefore, tenderable with appropriate 'price differentials' above or below the price of the basis grade. The unit of trading is fixed, i.e., contracts can be entered into only in the prescribed unit or multiples thereof. Delivery can be given by the seller during the delivery month on specified days known as 'tender days' and at specified delivery centres in addition to the centre at which the futures market is situated. The mechanics of trading, forms of contract, tenderable varieties, tendering differentials, etc., are all predetermined by rules, conventions or usages of the market. (For a typical 'futures or hedge contract' see Annexure V).

8. While actual delivery of goods can be given against the futures contract, usually the contract is not used for giving or taking delivery as it is primarily meant for providing insurance against price fluctuations. Deliveries take place only in a residual sense in respect of the outstanding contracts which are not offset by corresponding opposite transactions.

Sellers' options

9. The seller is given option to choose the date of delivery within the permitted period and the grade to be tendered from amongst the prescribed tenderable grades. The delivery can also be effected at any of the prescribed centres. These options with regard to grade, date and place of delivery are introduced to avoid corners and squeezes. A buyer may accumulate a large holding of futures contracts and at the same time acquire control of a large portion of the available ready quantity of the concerned commodity at a particular centre. In that case he would be able to squeeze the seller, i.e., to force the seller to settle the contract not at the competitive price determined by general bidding in the ring of the association but at the fancy price which the buyer dictates. This would have an undesirable effect on the level of futures prices in the ring as well as on the ready price of the commodity. The various options given to the seller make the contract broader and by increasing the volume of available supplies for giving delivery, if such a need for giving delivery arises, lessen the chances of any manipulation of the prices through futures trading.

Difference system

10. For the grades made tenderable against the futures contract, the bye-laws provide for payment of premia or discounts fixed with reference to the price of the basis grade. There are generally two systems for fixing such 'premia' and 'discounts' (called price differentials) known as the commercial difference system and the fixed difference system. Under the commercial difference system the premia or discounts are fixed on the basis of the actual differences in the ready prices of the contract grade and the tenderable grades, preferably everyday, during the delivery period. Under the 'fixed difference' system the premia and discounts are fixed in advance, often for all futures contracts of the season before the commencement of the season or sometimes before the commencement of trading in a particular futures contract. The commercial difference system is generally used in commodities like cotton and other fibres in which there are too many grades/varieties whose supply and demand conditions vary in relation to each other and as a result of which, the relationship between the prices of different grades/varieties and the basis grade cannot be predicted reasonably accurately. The fixed difference system is generally adopted in the case of oilseeds, grains, etc. where the different grades/varieties are not too many and the price differentials between different grades/qualities and the basis grade are reasonably predictable. Sometimes a compromise is made by fixing the price differences neither at the beginning of the season nor at the commencement of the contracts but before the beginning of the delivery period so that much of the uncertainty is removed.

11. The associations organising futures trading, generally called Futures Exchanges or Commodity Exchanges are membership organisations. The contracts are made between members of the Exchange and non-members can trade through or with members. The associations provide a trading hall (called a 'ring' or 'floor' or 'pit') for the members or their nominees and the price of a future contract is established through open bidding between these operators in the trading hall. They have detailed rules and bye-laws providing precise procedures to be followed in respect of all matters relating to trading under their auspices. The procedure for entering into futures contracts is illustrated in Annexure VI.

Hedging as insurance

12. Hedging is a form of insurance. The practice of hedging is based on the assumptions that (i) the ready and the futures prices of the commodity will move (i.e., advance or decline) together and (ii) the spread[1] between the ready and futures prices and between the prices of different futures contracts running concurrently will remain relatively stable. This is a tendency rather than a rule upon which hedgers can generally depend. The ready price and the futures prices of different futures contracts of the season ordinarily do move together in sympathy with each other because both ready and futures prices have to respond to the same basic demand and supply factors

[1]In the literature on futures trading often the spread between the ready and futures prices is also called 'basis' along with the 'grade' with reference to which the futures contract is entered. Thus the word 'basis' may either mean (*i*) the grade of the futures contract or (*ii*) the difference between the price of the commodity in the ready market and the price prevailing in the futures market depending on the context. In this Report, the word 'basis' is used only in the first sense.

since (i) futures contracts can be converted into actual commodity by taking or giving delivery of goods if either the buyer or the seller so desires and (ii) experienced traders constantly watch the relationship between ready and futures prices for arbitrage transactions.[1] In certain circumstances, the ready and futures prices may not move together. Moreover, sometimes the spread between the two may increase or decrease sharply. To the extent they do not move together by the same extent, hedging itself may be a source of minor gains or losses. However, by and large, hedging does afford adequate protection to the various functionaries.

'Short' and 'long' hedgers

13. The main aim of hedging is risk reduction. It involves commitments of opposite transactions in the related spot (actuals) and futures markets. Thus :

(i) A trader who acquires an unsold stock say of castorseed, *hedges* it *by selling* castorseed futures. He is 'long' in spot (actuals) and 'short' in futures and is called a short hedger.

(ii) An oil miller who sells castor oil to an exporter for actual delivery at some future date (ntsd contract) and does not have a stock of castorseed, may *hedge* his forward (delivery) commitment in the actual castor oil *by buying* castorseed futures. He is 'short' in spot (actuals) and 'long' in futures and is called a long hedger.

14. In each of these two cases, an open position in the spot market is 'off-set' by an opposite position in the futures market and when the open position in spot is terminated, the hedge is closed out by a reverse (offsetting) transaction in futures. Both these cases in quantitative terms are illustrated in Annexure VII. The different types of hedging are also described in this Annexure.

15. The volume of short hedging tends to be large when stocks in commercial hands are large and when the ready price is below the futures price; a reversal in this situation brings a decline. Conversely, the volume of long hedging is large when stocks are small and the ready price is above the futures price. Short hedging has a marked seasonal pattern, reaching a peak when commercial stocks are largest and the spread is favourable and then declining as the season advances. The seasonal pattern is less marked in long hedging. Generally there is an excess of short over long hedging during the bulk of the crop year.

Role of speculators

16. Hedging on futures markets cannot be practised unless there are operators willing to assume the risk which the hedgers desire to transfer. These operators are called speculators. A speculator operating on a futures market is one who buys or sells futures contracts without any corresponding commitments or transactions in the actual commodity with a view to making profit from the fluctuations in the prices. The basic distinction between hedge and speculative transactions on a futures market is that while in the case of a hedge transaction there is a corresponding opposite transaction in the actual delivery market, in the case of a speculative transaction, there is no corresponding transaction in the delivery market. While the motives of the speculator in entering into futures transactions are different from those of a hedger, the form or nature of transactions entered into by both on the futures market is similar. When a transaction takes place on a futures market, the transaction may well be between two hedgers or two speculators or between a hedger and a speculator. The speculators may be long or short speculators. The long speculators are those who expect the futures price to rise above the current level and assume risk by purchasing futures contracts. Short speculators are those who expect the futures price to fall and therefore are sellers of futures contracts. In a futures market, the total short selling position, made up of short hedgers and short speculators, and the total long buying position, made up of long hedgers and long speculators, must always be equal. Any excess of short over long hedging must be balanced by an equal excess of long over short speculation. Since short hedging exceeds long hedging for most of the crop year, hedgers are generally short and speculators, therefore, are generally long.

17. It is the ease with which speculation can be practised on the futures market that has given rise to much of the criticism against futures trading. There are, however, two inherently constructive or self-correcting elements in speculative activity in a futures market. First, it is in the interest of the speculators themselves to be well informed about the market conditions and important developments to avoid wrong decisions as such decisions are likely to result in heavy losses. It is this fear of losses which brings into operation their best judgement on the current and the prospective demand and supply situation. Secondly, the inefficient speculators, i.e. those who tend to make wrong forecasts, are bound to lose and get eliminated from the market.

Effects of futures trading on commodity prices

18. As regards the effects of futures trading on the ready prices of the commodity in which such trading is practised, two aspects on which attention has generally been centred, are (i) how the relationship between the ready or spot price and the futures price in a commodity is determined, and (ii) what are the effects of futures trading on the variability of ready price of the commodity.

(i) *Relationship between ready and futures prices*

19. The relationship between the ready price and futures price of a commodity is governed by the cost of carrying the commodity to the future date. The carrying cost is made up of storage and insurance charges, interest on the investment in the stock and the value of stocks lost due to deterioration and wastage. The ready and futures prices ordinarily run

[1]See paragraph 20 of this Chapter.

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parallel to each other subject to some spread between them determined by the carrying cost and conditions of supply and demand in the ready market.

20. In a properly functioning competitive futures market, the arbitrage activities, can always be relied upon to prevent the futures prices from exceeding the ready price by more than the net carrying cost. The arbitrageurs are operators who simultaneously purchase in one market at lower price and sell in another market at a higher price. If the futures price were higher than the ready price by more than the carrying cost, it would pay the arbitrageurs to sell futures in the futures market and at the same time buy the commodity in the ready market and carry it to the future date. This profitable business of arbitrage, of selling in futures and buying in ready and holding the stock of the commodity to the date of delivery in the futures market could be carried on until the increased demand for ready goods and increased supply of futures have brought down the futures price over the ready to an amount equivalent to the carrying cost so that there is no longer any profit in this kind of arbitrage business.

21. Arbitrage business, however, cannot be equally effective in preventing the futures price from exceeding the ready price by less than the carrying cost. In fact, it is possible that the futures price may not exceed the ready price at all or even fall short of the ready price even though the carrying cost is positive. It is of course true that as soon as the future price exceeds the ready price by less than the net carrying cost, holders of stocks would be in a position to make a profit by selling ready and buying futures instead of carrying the stock of the commodity to the future date. However, the volume of such arbitrage business of ready selling is limited by the amount of total stocks available for ready delivery in the hands of arbitrageurs. While in the first case, i.e. where futures price is greater than ready price plus carrying cost, any outsider with adequate credit and experience of the working of the futures market can step in by selling futures, buying ready and carrying the commodity to the future date, he cannot in the second case i.e. where futures price is lower than the ready price plus carrying cost, step in for selling ready and buying futures unless he is in possession of actual stocks of the commodity. Moreover, in the second case, the arbitrageur selling ready and buying futures may, if his seller delivers the good at a future date, end up with a stock of the commodity, the future value of which he does not know today.

(ii) *Effects on price variability*

(a) *Arguments in support of price stabilisation effect*

22. As regards price variability, the points to be taken into account are the frequency, the abruptness and the extent of variability. The traditional theory of speculation has claimed that while speculation increases the day to day frequency of fluctuation, it not only tends to level the prices throughout the year, i.e. reduces the extent of price fluctuations but also makes price changes over a short period less abrupt.

23. On an organised futures market, operators can come in large numbers and register their opinions continuously in the form of bids and offers. As a result, though changes in the prices are more frequent, such changes are less severe than where the market is not so well organised and the operators are spread out. The reasons for the frequent changes being graduated is to be found in the tremendous pressure brought to bear on both the supply and demand side of the market. The sellers, i.e. the shorts, are always trying to depress the market; buyers, i.e. the longs, are always trying to raise it. Moreover, for translating their desire into monetary gains or for preventive their monetary losses accumulating, sooner or later, the short sellers have to become buyers and the long buyers have to become sellers. As a result, just as soon as the price begins to fall there are shorts who begin to buy and just as soon as the price begins to rise there are longs who begin to sell, with a view to booking their profits. In other words, just as soon as the price begins to move in either direction, there are generally strong countervailing forces which hinder the price movement. As a consequence, abrupt and extreme changes in the price of a commodity, in which a well organised and highly competitive futures market is functioning, are generally avoided.

24. The reduction in the extent of seasonal variability, according to the traditional theory, is more or less, a direct result of the availability of hedging facilities and the constructive speculative activity on a futures market. In the absence of hedging facilities, in order to protect themselves from possible future price fluctuations, dealers in most agricultural commodities would restrict their purchases to the immediate needs of the processors or consumers of such commodities. They would not be inclined to make bulk purchases of the commodity in adequate quantity and store it for future needs in the later part of the season. There is, therefore, a distinct possibility of a sharp post-harvest fall in prices, when market arrivals of new crop are in full swing. On the other hand, when the hedging facilities are provided through futures markets, the dealers and stockists may undertake relatively larger purchases in the market and as a result the post-harvest slump in prices is slowed down. The possible excessive consumption during the immediate post-harvest period being checked and the commodity being carried forward for the later part of the season, the possible sharp rise during the later part of the season on account of the increasing scarcity of goods is also thereby prevented. The futures market may thus help the functionaries in the trade to perform the most important function of rationally distributing the available quantity of the commodity over the entire season. Hedging facilities may also help to some extent the carry-over of stocks from a bumper crop year to the next lean crop year, and thereby achieve a steadier level of prices over the two seasons. The mechanism of futures trading may thus achieve the co-ordination of the country's present and future expected supply with the present and future expected demand.

(b) *Arguments against price stabilisation effect*

25. The important arguments questioning the stabilising effect of futures trading on the prices of the commodity are as follows :

(i) The existence of a futures market tempts

persons with insufficient funds and little experience to trade through brokers who may be prepared to execute speculative orders at nominal brokerage charges. When such persons default on their obligations, they not only ruin themselves and their creditors but often give sharp jolts to the whole market.

(ii) The traditional theory assumes that the total speculative activity is only a small proportion of the total trading activity in the commodity. If, however, speculative transactions together form a large proportion of the entire trading activity in the commodity, such an activity may not have a stabilising effect on the prices as in that case the speculative activity will mainly determine the prices and will affect the buying and selling operations of those engaged in ready business.

(iii) The professional speculators use their superior judgement for forecasting the reactions of other speculators rather than the trend of non-speculative forces in the market. Their objective is not to make long-term forecasts but to foresee changes in the forecasts of the large number of small speculators in the near future and to outwit them by acting a little earlier.

(iv) Often speculators operating on a futures market follow the movement of prices and such 'movement trading' merely reinforces the price movement initiated for one reason or another instead of causing the prices to move on the basis of expert assessment of the current and prospective supply and demand situations.

(v) Often 'corners' or 'squeezes' can be engineered by large speculators and the prices can be artificially rigged up. A corner means that a person has secured a large portion of the available supply of a commodity or contracts in it and has a temporary monopoly. Cornering a futures market is easier than cornering a ready market because in the futures market, one can operate by investing a small amount and is not required to store the actual commodity.

26. The consensus of opinion is that while the stabilising effect of speculation on prices cannot be taken for granted in each and every case and under all circumstances, speculative activity in a properly organised, competitive and regulated futures market can serve the hedging needs of the functionaries engaged in the marketing of a commodity and can stabilise the prices of the commodity.[1]

Futures markets and cultivators

27. Futures trading can help cultivators in different ways. Those cultivators who grow commodities in very large quantities and have knowledge of the working of futures markets can use these markets for hedging their crops or stocks. Such hedging would benefit the producers directly and enable them to hold on to their stocks, spread out the sales of such stocks over a period and obtain a better average price for their produce. However, very few cultivators actually derive such benefits by direct use of a futures market for the following reasons. Very few producers raise crops which are large enough to compel them to think in terms of hedging. Generally the producers sell the bulk of their produce immediately after harvesting and do not carry any sizeable stocks. Most of the producers are illiterate and unfamiliar with the complicated technique of hedging. It may, however, be stated that in some regions like Saurashtra in Gujarat, where there is a long tradition of futures trading and the knowledge of such trading has percolated to producers also, the large producers do make use of futures market directly for hedging purposes. In order to ensure that the benefits of direct hedging accrue to the small producers, who are handicapped in availing of the facility for various reasons, many have felt the need for securing their participation through institutions like co-operative societies or Government agencies which arrange for the marketing of their crops.

28. Even if the cultivators do not participate in the futures market directly, such markets are beneficial to them in many ways. At the time of sowing operations a futures market serves as an advance indicator of the expected levels of prices during the marketing period and thus enables the cultivators to undertake proper crop planning. A properly organised and regulated futures market prevents any sharp decline in prices during the peak marketing period, when the cultivators sell the bulk of their crop. This enables the cultivators of that commodity to get a relatively better price for their produce than would be the case otherwise. The formation of a representative futures price and its dissemination throughout the country by modern methods of reporting and broadcasting enable the growers to realise a better price from the buyers of their produce. The integrated price structure which futures market promotes on account of arbitrage activities brings a more equitable return to the producers in different regions.

Futures markets and exports

29. Hedging facility is of invaluable help to exporters owing to various intricacies inherent in export business. An exporter can enter into an export contract only when there is a parity between the domestic and overseas prices. Such periods may even be as short

[1]Holbrook Working had examined intra-seasonal price variations in the US onion market in periods with and without futures trading (H.) Working, "Price Effects of Futures Trading", Food Research Institute Studies, Vol. I, No. 1, Feb. 1960). Pavaskar had likewise investigated the record of monthly and fortnightly price variations in the market for groundnut at Bombay. (M. Pavaskar, "Futures Trading and Price Variations", Economic & Political Weekly, Vol. VIII No. 9, February 28, 1970). The statistical findings of both these studies are that spot prices fluctuate less widely in the presence of futures trading than in its absence. Subsequently, Naik found that not only the short-term price movements, but also the seasonal price variations in the spot groundnut market at Bombay were lower during the years with futures trading than during those without such trading. (A.S. Naik, "Effects of Futures Trading on Prices", Somaiya, 1970). Similar studies made in the office of the Forward Markets Commission in respect of certain commodities also reveal the stabilising influence of futures trading on prices (see Annexure VIII).

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as a few hours. During such periods he has to offer his goods simultaneously to a number of likely buyers and then on acceptance of his offers by them or their orders by him, he is obliged to contract for the delivery of goods at a fixed price for delivery at a later date. Normally a shipper does not hold large stocks in anticipation of foreign demand or buy actual goods immediately on the acceptance of his offers at the prevailing price long ahead of shipment for various reasons. In the first place, he may not have the necessary facilities to store the goods in good condition. Secondly, such stocking or buying in advance would involve locking up of considerable funds increasing his cost. Thirdly, in certain cases, the goods may not be available for purchase immediately but may become available only just prior to the shipment date. This generally is the case when foreign bids are received before the commencement of the marketing period of an agricultural commodity or its processed product. Fourthly, it may not be economical for an exporter to enter the ready market for purchasing any large quantity of the commodity at any one point of time as it may itself lead to a price rise in the market.

30. Besides providing hedging facilities, the futures market supplies quotations for different future delivery periods based on the expert assessment of the anticipated future supply and demand. The existence of such quotations enables the exporters to quote to foreign buyers prices for different shipments ahead. Being assured of their normal profits because of the insurance service of the futures market, the exporters are in a position to trade on a smaller margin of profit which increases their competitive capacity in the world markets.

31. The facilities provided by the futures market thus help to increase foreign exchange earnings by raising exporters' competitive capacity, reducing their costs and enabling them to seize every opportunity to export whenever there is parity between domestic and overseas prices. The existence of futures markets in export commodities also facilitates the participation of small traders in the international trade. Futures markets can, therefore, be considered as one of the instruments of export promotion.

Role of futures trading in commodities subjected to management schemes

32. The question arises as to what would be the role of futures trading in the commodities in which the Government have introduced or propose to introduce schemes of management with a view to helping producers to get remunerative prices, evening out price fluctuations or ensuring the availability of the commodity to consumers at reasonable prices. Such schemes of management generally take the form of (a) monopoly procurement schemes—whereunder the State procures the commodity from producers at a fixed price, undertakes its sales and distributes profits among the producers, (b) price support programmes at levels fixed by the Government and (c) building up of buffer stocks to even out price fluctuations and ensure availability during the lean period. In certain commodities, cooperative organisations of producers also play a significant role at the primary marketing stage of the commodity.

33. While considering the question whether futures trading facilities are necessary under such conditions, a distinction should be made between full-fledged physical control on production and distribution of the commodity and the schemes of management of the bove types. Most of these schemes, introduced to influence the market behaviour in a desirable way, cover only a part of the production and distribution of the commodity but leave a sizeable proportion of these activities in private hands. There is no scope for futures trading in any commodity if there is complete control of the State on its supply and distribution. However, if the private trade is free to procure a large part of the supply and handle its marketing, it has to carry forward stocks of the commodity and for this purpose it would need hedging facilities. Even if the State procures entire supply from producers but sells it to the private trade for its distribution, the trade interests would need hedging facilities.

34. In India, in most of the commodities, at present, the control is indirect with a view to influencing the market behaviour and substantial part of the supplies and marketing are left in the hands of the private trade. Under the price support programme, the State or its agencies are committed to purchasing the commodity only when the price of the commodity tends to fall below the prescribed support prices. Futures trading is not incompatible with such programme. First, the objective of such price support programme is to assure producers of minimum remunerative prices which are largely determined by the cost of production and there is considerable scope for determination of fair competitive prices above these minimum levels and there is no reason to deprive farmers of higher prices above these levels if properly organised futures trading can help them to receive such prices. Moreover, the range of fluctuations even in the commodities in respect of which such support prices are announced is often quite large. Buffer stock schemes are also not incompatible with futures trading. The principal aim of buffer stock scheme in a commodity is to stabilise the prices of the commodity by withdrawing its supplies from the market during bumper crop years or peak marketing periods and releasing them into the market during short crop years or lean marketing periods. Such a scheme, if successfully operated, would reduce price fluctuations both inter-season and intra-season. However, even when there is buffer stock scheme in a commodity, if the major part of the crop is to be marketed by the private trade, the need for insurance facilities through futures trading would still be there, as there would be a good deal of uncertainty about the buying and selling policies of the buffer stock agency and about the extent to which it will be able to reduce possible fluctuations in the prices.

35. In fact, the existence of futures markets in commodities in which the Government have introduced 'Management Scheme' of the above type will be quite helpful to the proper implementation of the schemes. In most of these schemes, the agencies operating them have to face the same problems in regard to the management of the stocks procured by them as faced by the private trade viz., the possibility of fall in the prices at a future date and planning their disposal

taking a view of the future trend of prices. If a futures market exists, they can hedge their stocks to protect themselves against any possible fall in prices. Even if they do not use the futures market for hedging, the availability of futures prices would be of immense value to them for deciding upon their buying and selling policies as also the quantum of stocks to be held.

36. Right from the beginning, futures trading came to be organised under the auspices of an association with detailed rules, regulations and procedures. This was mainly because its organisation and management could not be left to the vagaries of a few individuals or small groups and that a scrupulously impartial management of such trading in the interests of all participants was considered desirable. However, the need for additional regulation to ensure that the speculative activities at such associations remained constructive and not excessive or manipulative was felt from time to time to safeguard the public interest. Both producers and consumers were affected by the happenings on the futures markets. While a properly operated futures market was likely to give a relatively better price to producers and keep consumers' price low by reducing distribution costs, an improperly operated futures market was likely to depress producers' price and raise the consumers' price. Adequate participation of speculators was no doubt useful for promoting hedging but their activities needed to be monitored to prevent dissemination of false or misleading market information and manipulative activities in the market. Demands were voiced in many countries that the Government, either directly or indirectly, should supervise the working of futures trading associations with a view to maintaining healthy competition, preventing manipulations and ensuring fair trading practices. These demands have been met in most of the countries where futures trading is practised by passing suitable legislations to meet their requirements. In India such trading came to be increasingly regulated by the Government from the days of the Second World War. A comprehensive review of the regulation of futures trading in India is given in the following Chapter.

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CHAPTER 3

REGULATION OF FORWARD TRADING IN INDIA

Historical background

There is a long tradition of futures trading in India going back, in the case of some commodities, to over a hundred years. However, futures trading in a well organised form seems to have developed as a consequence of large scale fluctuations in prices experienced after the first World War.

2. Cotton, perhaps being an exportable commodity, seems to have attracted futures trading in an unorganised form well before 1875. A representative association called the East India Cotton Association was formed in 1921 to organise such trading in cotton on proper lines. This was perhaps the first futures trading association in India with a comprehensive constitution and bye-laws providing for all details. Other commodities in which futures trading has traditionally been conducted for a long time include oilseeds, raw jute and jute goods, spices like pepper and turmeric and bullion.

3. During the early years of World War II, the prices of various commodities rose to high levels as a result of acute shortages and the Government of India issued orders under the Defence of India Rules prohibiting futures trading in most of the commodities like foodgrains, cotton, edible oilseeds and oils, jute goods, etc. With the cessation of hostilities, there was an increasing demand for removal of ban on futures trading in various commodities. However, the general consensus was that futures trading in important commodities should be permitted only under Governmental regulation in public interest.

4. The first comprehensive measure for the purpose of continuous regulation was taken in the erstwhile Bombay State in 1947, when the Bombay Forward Contracts Control Act was enacted. The act was a permissive one and was applied to cotton, oilseeds and bullion in the city of Bombay. It vested certain regulatory powers in the State Government but did not set up any independent body specifically for exercising them. After independence, stock exchanges and futures markets were included in the Union List of powers under the new Constitution and it was decided to undertake central legislation on the subject. In February 1950, the Futures Markets (Regulation) Bill was drafted and circulated to State Governments, Chambers of Commerce, the Reserve Bank of India, and other interests for eliciting their views. The draft bill was later referred to an Expert Committee under the Chairmanship of Shri A. D. Shroff, which suggested various modifications. The basic approach of the Expert Committee in regard to forward trading has been clearly set out in the following :—

"To start with, there are certain general propositions which must be agreed upon before any scheme for regulating forward markets could at all be considered. Forward trading involves speculation about the future, but not all forms of forward trading could be considered as either unnecessary or undesirable for the efficient functioning of anything but the most primitive economy. With the development of international communications, it has become virtually impossible in normal times for any of the principal commodity markets of the world to function in isolation from the rest at any rate in respect of those commodities which constitute the staple lines of world commerce. The price system is not merely subject to world influences but also to influences emanating from unforeseen variations in demand and supply over a period of time. It is an inevitable characteristic of modern industrial civilisation that it involves a lengthening of the process of production, and this increases the risks inherent in any productive enterprise. Most persons engaged in productive enterprises have frequently "to take a view of the market". The same applies to persons engaged in purely trading activities. To the extent to which forward trading enables producers, manufacturers and traders to protect themselves against the uncertainties of the future, and enables all the relevant factors, whether actual or anticipated, local or international, to exercise their due influence on prices, it confers a definite boon on the community, because, to that extent, it minimises the risks of production and distribution and makes for greater stability of prices and supplies. It must be recognised, therefore, that forward trading plays a useful role in modern business. At the same time, it must be admitted that this is an activity in which a great many individuals with small means and inadequate knowledge of the market often participate in the hope of quick or easy gains, and consequently, forward trading often assumes unhealthy dimensions, thereby increasing, instead of minimising, the risks of business. There are forms of forward trading, for example, options, which facilitate participation by persons with small means and inadequate knowledge. In conditions of shortage or surplus, prices may assume only a one way trend, and forward trading may accentuate such trend, to the serious detriment of the interests of the community. It

is, therefore, necessary to eliminate certain forms of forward trading, and permit others under carefully regulated conditions, in order to ensure that, while producers, manufacturers and traders will have the facilities they need for the satisfactory conduct of their business, the wider interests of the community, and particularly, the interests of consumers, will be adequately safeguarded against any abuse of such facilities by others."[1]

5. The Expert Committee in keeping with its approach made detailed recommendations regarding the scheme of regulation of different types of forward contracts including futures contracts. A fresh bill on the basis of the Expert Committee's recommendations, was introduced in Parliament in December 1950, and after undergoing some changes at the Select Committee stage, it was placed on the Statute Book in December 1952, as the Forward Contracts (Regulation) Act, 1952 (FC(R) Act).

Classification of contracts and the scheme of their regulation under the FC(R) Act

6. The scheme of the classification of different types of contracts adopted under the FC(R) Act is as follows :—

(i) **Ready Delivery Contract**—Ready delivery contract is defined as a contract which provides for delivery of goods and payment of a price therefore either immediately or within such period not exceeding 11 days after the date of the contract and subject to such conditions as the Central Government may, by notification in the Official Gazette, specify in respect of any goods, the period under such contract not being capable of extension by the mutual consent of the parties thereto or otherwise. Some reasonable period has to be provided for giving and taking delivery of goods even against the contract to be completed immediately as commodities are often bulky and in the wholesale market, where they are dealt in, immediate delivery across the counter is not possible as the process of drawing samples, weighing goods and transporting from the buyer's godown to that of seller, takes time. In the FC(R). Act, the period provided for this purpose is 11 days.

Such ready delivery contracts are outside the purview of the FC(R) Act. The above definition of the ready delivery contract was amended in October 1971 by adding the provisos shown in Annexure IX in order to ensure that such contracts were performed by giving and taking actual delivery and were not used for conducting, under their guise, futures trading.

(ii) **Forward Contract**—Forward contract is defined as a contract for the delivery of goods and which is not a ready delivery contract.

(iii) **Specific Delivery Contract**—Specific delivery contract is defined as a forward contract which provides for the actual delivery of specific qualities or types of goods during a specified future period at a price fixed thereby or to be fixed in the manner thereby agreed and in which the names of both the buyer and the seller are mentioned.

(a) **Non-transferable Specific Delivery Contract**—Non-transferable specific delivery contract is defined as a specific delivery contract, the rights or liabilities under which or under any delivery order, railway receipt, bill of lading, warehouse receipt or any other document of title relating thereto are not transferable.

(b) **Transferable Specific Delivery Contract**—Transferable specific delivery contract is defined as a specific delivery contract which is not a non-transferable specific delivery contract and which is subject to such conditions relating to its transferability as the Central Government may, by notification in the Official Gazette, specify in this behalf.

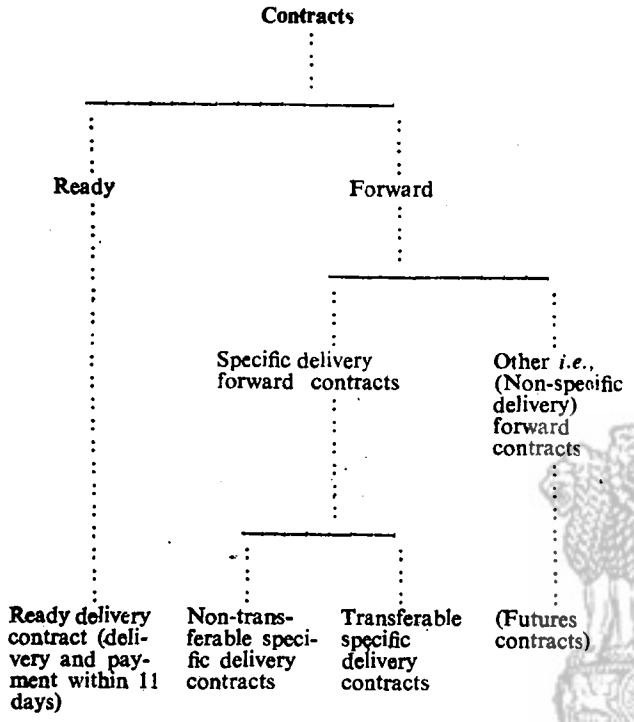
7. The non-transferable specific delivery (ntsd) contracts are contracts which in foreign literature are often referred to as 'time contracts' or 'contracts for deferred delivery' or even 'spot contracts'. The ready and ntsd contracts, having been entered into for giving and taking actual delivery of goods, the concerned sellers or buyers are not supposed to dispense with actual delivery except under 'force majeure' (i.e. acts of superior powers like God, Nature or State as a result of which giving or taking delivery becomes impossible) or to transfer the contracts to third parties. If any of the parties to contracts fails to give or take delivery, the other party can sell or buy the actual goods at the cost of the defaulting party. The futures contracts on the other hand, can be readily transferred by buyers or sellers to other parties, since such contracts are not entered into to give or take actual delivery of goods. In a transferable specific delivery (tsd) contract, the original parties to the contract can transfer their rights or liabilities under the contract or under the document of title relating there to any third party who in turn can also transfer his rights or liabilities to another party. Such transfers can continue unless the total number of transfers is restricted. As a consequence, the actual delivery of goods is between the final seller and the final buyer while all earlier parties settle the contracts by payment of price differences. The tsd contract was introduced as a separate category of contracts in the FC(R) Act, as it was urged by the trading community that in many trades, particularly in jute trade, such contracts were used for ordinary non-speculative commercial transactions and were performed by issuing transferable delivery orders .

8. The FC(R) Act is an enabling measure in the sense that its regulatory provisions can be applied by notification to different types of forward contracts in specified commodities and specified areas. It enables the authorities normally to regulate trading in all

[1]Report of the Expert Committee on the Futures Market (Regulation) Bill, 1950—paragraph 2.

types of transferable contracts i. e. both futures (or hedge) as well as tsd contracts. It, however, provides for the exclusion of tsd contracts and the inclusion of ntsd contracts in the ambit of regulation if the circumstances so warrant. The Act prohibits 'options' in all goods.

9. The scheme of classification adopted in the FC(R) Act may be tabulated as follows.



10. The principal characteristics of the above scheme of classification of contracts are (i) ready delivery contracts as defined in the FC(R) Act, have been kept outside the purview of the Act, (ii) the 'futures contracts' have not been defined in the Act but by implications indicated as transferable non-specific delivery forward contracts, (iii) both ready delivery contracts and ntsd contracts have been considered to be akin to each other but while ready delivery contracts have been kept completely outside the purview of the FC(R) Act, ntsd contracts, though ordinarily to be exempted from regulation being contracts for taking and giving actual delivery of goods, the Government have taken power under the Act to make the provisions of the Act applicable to such contracts if it were of the opinion that it was in the interest of trade or in the public interest to regulate and control such contracts, and (iv) tsd contracts have been bracketed with futures contracts but can be exempted from regulation under special circumstances.

11. The above approach to the classification and regulation of various types of contracts in the FC(R) Act is based on the recommendations of the Expert Committee. The said Committee felt that although the futures contracts have in practice certain distinguishing characteristics of their own, in formal appearance there may be very little to distinguish them from tsd contracts. It, however, refrained from distinguishing futures contracts on the basis of such characteristics and limiting the scope of the Bill to such contracts only because in the majority opinion of the Committee there was a distinct possibility of ntsd contracts being used as futures contracts for all practical purposes, with a view to evading the law. The Expert Committee conceded that while there was a need for separate category of tsd contracts in certain trades such as jute, it felt that since exclusion of such contracts from the scope of the Bill might lead to evasion in most of the trades while their inclusion might be found unnecessary only in a few trades, the proper course would be to include such tsd contracts as a rule, but to provide for their exclusion in special cases, where Government were satisfied about their special conditions, and for such period as might be necessary.

12. According to the Expert Committee, ntsd contracts were in a different category since such contracts could not normally be used for speculative purposes. While admitting that its attention was drawn to the instances in which speculation was taking place on the basis of ntsd contracts, the Committee came to the conclusion that it would cause serious inconvenience to trade and make normal trading practically impossible if such contracts are not exempted from the restrictions applicable to the contracts of other two types (i e. futures and tsd contracts). The Expert Committee, therefore, recommended that while the scheme of regulation envisaged in the Bill should apply to futures contracts and tsd contracts, the Government should have powers to (a) exempt tsd contracts where their inclusion is likely to cause unnecessary hardship or inconvenience to the trade concerned, and (b) impose such regulation as it might deem fit on ntsd contracts where there is positive evidence that their exclusion from the scheme had encouraged practices likely to defeat the purpose of the Bill.

13. The experience gained by the Forward Markets Commission in the course of regulation of forward markets has shown that the above cautious and flexible approach adopted by the Expert Committee which enables regulation or prohibition of all types of forward contracts, if the circumstances so warrant, has been broadly correct. The Commission found that whenever futures trading in the commodities permitted at the recognised associations was subjected to stringent restrictions or suspended or prohibited altogether, futures trading continued to take place in these commodities in two ways. One was to invoke the name of ntsd contracts, which were free, to camouflage trading in futures or tsd contracts which were not free in the commodities. Though the forms of the contracts etc., used for the purpose described the contracts as ntsd contracts, in actual practice, the contracts were like futures contracts, transferred and finally settled by payment of differences without giving or taking delivery. Another was to conduct futures trading in a banned commodity in the name of a commodity to which the provisions of the Act had not been applied. Enforcement action against such activities became difficult or very protracted in view of certain loopholes in the relevant provisions of the Act which came to light during the course of prosecutions. As a result, in a large number of commodities, the Government, on the

advice of the Forward Markets Commission had to (i) prohibit altogether or regulate trading in ntsd contracts, which were ordinarily to be exempted from the purview of the Act, and (ii) prohibit trading in tsd and futures contracts which were earlier free.

14. The scheme of regulation under the FC(R) Act envisages a three-tier system of control. The three authorities which control futures trading are (i) recognised and registered associations, (ii) the Forward Markets Commission and (iii) the concerned Ministry of the Government of India.

Recognised and registered associations

15. When the Commission considers either on the basis of representations received or on its own that forward trading in a particular commodity needs to be regulated or prohibited, it undertakes the study of that commodity, consults the various concerned interests and authorities and submits a report to the Government recommending application either of section 15 or of section 17 of the Act. While recommending application of section 15, the Commission also recommends to the Government grant of recognition to suitable associations at suitable centres for conducting forward trading. In the commodities to which the provisions of sections 15 or 17 of the Act have not been applied, forward trading can be conducted subject to the restriction that if such trading is controlled or regulated by an association, such association must have obtained a certificate of registration from the Commission under section 14B of the FC(R) Act. The requirement of registration was introduced in December 1960 to enable the Commission to keep a watch on all the associations conducting forword trading in the commodities to which the concerned sections of the Act had not been applied.

Instruments of regulation

16. In the task of regulating futures trading in various commodities the Forward Markets Commission was influenced mainly by three considerations viz., need to (i) curb unhealthy speculation and manipulative tendencies, (ii) avoid risk of defaults and (iii) prevent any runaway tendency in futures prices due to any excessive speculative activity in the futures market. The broad approach adopted by the Commission in regulating futures markets was that there should be self-regulation by the recognised associations and the Commission should step in only when the associations either failed to act or the action taken by them was inadequate to meet the needs of the market situation. From this view point, the bye-laws of the recognised associations were so framed as to give adequate powers to the Boards of Directors of recognised associations as well as the Commission.

17. The major instruments of control for regulating futures trading at the recognised associations from the above point of view, which could be employed by the Boards or the Commission under the Bye-laws, were (i) special or automatic clearings, (ii) ordinary margins, (iii) special margins, (iv) postponement of outward payment of profits, (v) limits on price fluctuations, (vi) limits on open position, (vii) maximum and minimum prices, (viii) prohibition of fresh trading, (ix) suspension of futures trading for a specified period; and (x) closing out the outstanding contracts. These have been explained at length in Chapter V of the Report of the Forward Markets Review Committee appointed in 1966 under the Chairmanship of Prof. M. L. Dantwala (Dantwala Committee).

Regulation of ntsd contracts

18. In keeping with the intention of the Act, the Commission, during the initial years of regulation, recommended application of section 15 to forward contracts other than ntsd contracts. As a result, without obtaining recognition, any association could conduct trading in ntsd contracts provided such contracts were for actual delivery. However, subsequently, whenever futures trading in various commodities at the recognised associations was subjected to stringent regulatory measures or suspended or prohibited, ntsd contracts came to be increasingly used for camouflaging futures trading in those commodities. As such misuse of ntsd contracts could not be checked due to certain loopholes in the definition of ntsd contracts, the Government, on the advice of the Commission had to either regulate or prohibit ntsd contracts also in a large number of commodities under section 18(3) of the Act.

Registered associations

19. The category of registered associations was introduced by an amendment to the FC(R) Act in December 1960 to enable the Commission to have a census of all the associations concerned with forward trading and to monitor their activities. The Commission's experience of the working of registered associations has not been happy. They tried to conduct futures trading in various banned commodities either in the guise of ntsd trading or futures trading in free commodities and the Government had to prohibit all forward trading in most of these commodities.[1] At present most of the registered associations are inactive as forward trading in the commodities for which they were registered has either been prohibited or suspended.

Enforcement

20. Apart from regulation, the major concern of the Commission particularly during the past few years when forward trading in many commodities came to be banned, has been with the enforcement of the penal provisions of the FC(R) Act.

21. Unfortunately, the Commission was handicapped in this task right from the beginning. None of the provisions made under the FC(R) Act empowers the Commission to directly deal with illegal forward trading. The responsibility for the enforcement of the penal provisions of the Act in respect of illegal trading is primarily that of the State Police Authorities as such trading constitutes offences most of which are cognizable. Rule 13 of the FC(R) Rules, however, enjoins on the Forward Markets Commission to communicate information in respect of the commission of

[1]See paragraphs 15 and 16 of Chapter 7.

any offence under the Act to the concerned authorities and assist such authorities in scrutinising the documents referred to by them and in rendering such expert advice as may be required by them. This rule was introduced in October 1971, at the instance of the Commission, when the right of its officers to give evidence in the course of prosecutions launched under the Act by the State Police Authorities was challenged.

22. In spite of the above position in law, the Commission was required to concern itself with the problems of illegal forward trading right from the beginning, as it was obvious that prevention of illegal trading was **sine qua non** of successful regulation. It was also realised the owing to technical and complicated nature of the offences, left to themselves, the State Police Authorities preoccupied with law and order, would be unable to make any headway with the prevention of illegal forward trading. The individual citizens as well as public bodies and even the State Governments had come to look upon the Commission as an organisation primarily responsible for dealing with all aspects of forward trading. Consequently, complaints relating to illegal forward trading were generally made to the Commission instead of to the State Police Authorities.

23. In 1956, therefore, the Commission set up a small separate section to collect information about illegal forward trading and to pass it on to the State Police Authorities for necessary action. In course of time, the Commission established an Enforcement Directorate with a senior police officer of the Indian Police Service as its Director. The considerations which weighed with the Commission in associating a police officer with it were that such a senior officer would be in a better position to establish liaison with the State Police Departments all over the country and impart the necessary professional touch to the task.

24. The Enforcement Directorate of the Commission is, however, not an instrument of enforcement in the sense in which similar Directorates set up under other Acts such as Foreign Exchange (Regulation) Act, Income Tax Act, etc. function. It has no powers under the FC(R) Act either for search or seizure or for adjudication of offences under the Act. Even the Director of Enforcement, who is a police officer, is divested of his police powers on his appointment as Director. The functions of the Enforcement Directorate are limited to (i) activating the police authorities to take action against illegal forward trading, (ii) assisting them on the technical side of the investigation of the offences under the Act and (iii) giving expert evidence in the courts of law in the course of prosecutions launched by the State Police Authorities under the Act. In practice, however, the officers of the Enforcement Directorate play a much more active role in relation to illegal forward trading. They collect and verify information about illegal forward trading by visiting centres of such trading and cultivate local informants, organise raids by the police on the premises of the parties conducting illegal forward trading, assist the police in seizure of the relevant incriminating documents during the raids, scrutinise the documents and prepare prosecution cases, assist the prosecuting officers during trial of the cases and tender expert evidence on behalf of prosecution, study the judgements delivered in the cases so as to suggest revisions and appeals in suitable cases, prepare draft affidavits in cases of writ petitions filed by affected parties etc.

25. The Enforcement Directorate of the Commission also conducts at regular intervals training courses for the benefit of police and prosecuting officers of the State Governments to familiarise them with various aspects of forward trading, investigation and prosecution of the cases under the Act and scrutiny of the documents seized during the raids.

26. Mainly as a result of the efforts of the Enforcement Directorate since 1957, 1239 raids have been conducted and 1914 cases registered under the FC(R) Act in different parts of the country till 31st March, 1980. The details of these are at Annexure X. A large number of these raids have been conducted by the police authorities of different States at the instance of the Enforcement Directorate and with active assistance of its officers. Of late, the police authorities, in certain parts, particularly in Gujarat and Delhi, have started initiating action against illegal forward trading on their own. The problem of illegal forward trading has, however, grown in scope and complexity as a result of extension of prohibition on forward trading to a large number of commodities and ingenious methods adopted to circumvent the same. In any concerted effort to check illegal forward trading, the Commission would have to continue to play a major role. This would require strengthening of the Enforcement machinery of the Commission.

CHAPTER 4

COMMODITIES SUITABLE FOR FUTURES TRADING UNDER PRESENT CONDITIONS

In this Chapter, the Committee has considered the desirability of permitting futures trading in different commodities under present conditions. The commodities selected for this purpose are those in which there has been a tradition of futures trading and in some of which such trading has been suspended from time to time and also those commodities in which there has been a demand for introducing futures trading. While we have examined most of these commodities in detail and made specific recommendations, in certain other commodities in which futures trading may be beneficial, we have suggested further exploratory studies.

I. Foodgrains—Cereals and Pulses

2. Forward contracts of all types (i.e. futures as well as transferable and non-transferable specific delivery contracts) in foodgrains have remained banned since 1942 under various statutory orders and since January 1955, under the FC(R) Act.

3. Forward trading in foodgrains was not permitted mainly because of the short supply conditions in these commodities in relation to demand year after year and consequential measures such as physical controls, zonal restrictions on movements, etc., from time to time. The short fall in supplies had to be met by large imports till June 1976. However, with the advent of the green revolution, a quantitative as well as qualitative change has come about in the production of cereals mainly wheat and rice since 1967-68. The adoption of high yielding varieties and technological innovations brought about revolutionary changes, the impact of which was felt particularly in wheat. The trends in production of cereals may be seen from the following table :—

('000 tonnes)

Season		Wheat	Rice	Others	Total
1950-51	..	6,462	20,576	15,376	42,414
1958-59	..	9,958	30,847	23,187	63,992
1964-65	..	12,257	39,308	25,374	76,939
1967-68	..	16,540	37,612	28,798	82,950
1975-76	..	28,846	48,740	30,409	1,07,995
1976-77	..	29,010	41,917	28,879	99,806
1977-78	..	31,749	52,670	30,015	1,14,434
1978-79 (Final)	..	34,982	53,829	30,389	1,19,200

Source—Directorate of Economics and Statistics, Ministry of Agriculture & Irrigation, Government of India.

The country has emerged from a long period of shortages to an era of adequacy although at a low level of demand. The stocks of cereals with the Government agencies have been maintained at a fairly high level reaching about 20 million tonnes in 1978-79. Although the stocks have come down recently due to significant short fall in the production of cereals in 1979-80, they are nevertheless at a satisfactory level. It may be mentioned that cereals, mainly consisting of wheat and rice are the backbone of the public distribution system. About 8 to 10 million tonnes of cereals are sold through 2.47 lakh fair price shops per annum at a more or less uniform price all over the country and a large quantum is further being distributed under 'Food for Work' programmes. As a result, the prices of cereals have remained generally stable.

4. Pulses, on the other hand, present an entirely different picture vis-a-vis that of cereals. The production of pulses has remained stagnant over the years around 12 million tonnes as will be seen from the table below :—

('000 tonnes)

Season		Gram	Tur	Others	Total
1950-51	..	3,651	1,719	3,041	8,411
1958-59	..	7,023	1,702	4,424	13,149
1964-65	..	5,777	1,890	4,750	12,417
1967-68	..	5,971	1,741	4,390	12,102
1975-76	..	5,879	2,099	5,061	13,039
1976-77	..	5,424	1,725	4,212	11,361
1977-78	..	5,410	1,930	4,632	11,972
1978-79 (Final)	..	5,835	1,914	4,421	12,170

Source—Directorate of Economics & Statistics, Ministry of Agriculture & Irrigation, Government of India.

5. In view of the persistent shortages experienced in the supplies of pulses during the last many years, exports of this item remained banned . In order to augment domestic supplies, imports of pulses have been placed on OGL from April 1978. However, in view of higher prices prevailing in other countries, imports of pulses have not been feasible to any significant extent. With inadequate production within the country, inability to obtain the requirements from abroad and absence of any new technological developments, the shortage situation in pulses is expected to continue in the years to come. Hence the prices of pulses have been showing a rising trend.

6. The interests representing foodgrains who gave evidence before the Committee did not press for the facility of futures trading. Foodgrains being commodities of mass consumption have been subjected, for very good social and economic reasons, to fairly

thorough regulations and control through such measures as support price fixing, retail price fixing, procurement, buffer stock operations and organisation of ration shops in an extensive public distribution system. As our criteria have shown in an earlier Chapter, such commodities cannot be a fit material for trading in the futures markets. Keeping this in view and also what is stated above, the Committee recommends that unless this sector has developed large surpluses to the extent, of enabling the country to undertake regular exports, it would not be advisable to permit futures trading in foodgrains. The question of permitting ntsd contracts in foodgrains has been discussed in Chapter 6.

II. Cotton and Kapas

7. Futures trading in cotton is not being permitted since 1st September, 1966. Prior to that, it was conducted under the auspices of associations recognised under the FC(R) Act at Bombay for all varieties grown in the country and at Ahmedabad, Ujjain and Akola for varieties grown in the respective regions. Trading in non-transferable specific delivery (ntsd) contracts in cotton is being regulated all over the country under the auspices of nine associations at Bombay, Ahmedabad, Surat, Baroda, Surendranagar, Bhatinda, Ujjain, Guntur and Coimbatore recognised from time to time. Futures trading in kapas which was permitted in Gujarat at Surendranagar and Dhrangadhra and in Punjab at Bhatinda and Dhuri since 1964, was suspended on 4-12-1970.

8. While kapas (unginned raw cotton) is harvested and marketed for a short span of three to four months, the full-pressed bales of cotton lint available after ginning are marketed continuously throughout the seasons. Thus, while kapas has to be held by the producers, the village merchants and the ginners, cotton is being held by the upcountry merchants, the merchants of the terminal markets and the mills for consumption within the country.

9. Cotton was subjected to Government control from 1943-44, when the floor and ceiling prices were fixed by the Textile Commissioner. The floor and ceiling prices were abolished in September 1967 and were replaced by support prices. The Cotton Corporation of India (CCI) was established in July 1970 as a canalising agency for import of cotton and for purchase, sale and equitable distribution of indigenous cotton. To start with, the CCI undertook the whole of import business in cotton while its activity relating to indigenous cotton remained restricted till about 1977-78, when for the first time it purchased 6.50 lakh bales of indigneous cotton. In 1978-79 its purchases rose to 10.38 lakh bales (about 11 per cent of the production) and it has proposed to purchase 15 lakh bales (about 20 per cent of the expected production) during 1979-80. The Maharashtra State Co-operative Marketing Federation (MSCMF) which acts as the agent of the Government of Maharashtra under the monopoly procurement scheme, introduced in Maharashtra in 1972-73 season, entered the field of marketing of cotton to enable the growers to get remunerative prices for their kapas. It procures cotton to the extent of 14 to 18 lakh bales depending upon the production in the State.

10. The supply and demand situation obtaining in cotton during the last 10 years since 1969-70 is shown in the following table :—

(*Lakh bales of* 170 *kg each*)

Particulars	Season (September—August)										
	1969-70	1970-71	1971-72	1972-73	1973-74	1974-75	1975-76	1976-77	1977-78	1978-79	1979-80
Opening stocks	19.6	19.6	19.2	30.4	29.7	23.7	28.8	15.5	13.7	21.0	27.3*
Commercial crops	61.4	56.7	74.1	66.3	66.5	73.6	66.5	59.5	72.4	79.3	78.5
Imports	9.6	8.9	7.9	4.7	1.9	1.4	1.3	8.2	3.1	0.3	..
Total availability	90.6	85.2	101.2	101.4	98.1	98.7	96.6	83.2	89.2	100.6	105.8
Mill consumption	67.4	62.7	67.3	68.7	72.3	67.2	75.6	67.5	66.2	70.5	73.0
Ex-factory consumption ..	1.0	1.1	1.1	1.1	1.1	1.6	1.5	2.0	2.0	2.5	2.5
Exports	2.6	2.2	2.4	1.9	1.0	1.1	4.0	Nil	Nil	2.9	6.6
Total disappearance	71.0	66.0	70.8	71.7	74.4	69.9	81.1	69.5	68.2	75.9	82.1
Closing stocks	19.6	19.2	30.4	29.7	23.7	28.8	15.5	13.7	21.0	24.7	23.7

Source—Indian Cotton Annual—East India Cotton Association (EICA), Bombay, from 1969-70 to 1973-74. Cotton Advisory Board (CAB) from 1974-75 to 1979-80. Figures for 1979-80 are as on 14th May 1980.

*Adjusted by the CAB on 14-5-80; the closing stocks figures for the previous years have not been adjusted.

11. It will be seen that there was a large variation in the production of cotton during the last one decade. The average production during the last three seasons has been quite high around 77 lakh bales as against the average consumption of about 72 lakh bales for the same period. With the introduction of compulsory usage of man-made fibres in the manufacture of cotton textiles from January 1977, which enabled substitution of man-made fibres in place of cotton, the pressure of demand on cotton softened considerably. As a result, the end-season stocks have been quite sizeable. The imports of cotton, which were undertaken with a view to bridging the gap between the internal supply and demand, have been practically eliminated during the last three years. Further, the exports of stable cotton, which had remained prohibited during the last 20 years, have been permitted through export quotas from time to time to State Agencies like CCI and MSCMF and to a small extent to co-operative societies which were holding huge stocks of such cottons for a long period.

12. Thus, a material change has come about in the supply and demand situation of cotton since futures trading was prohibited for the first time in the season 1966-67. During that year, cotton production was hardly 53 lakh bales as against the 78.50 lakh bales in the 1979-80 season. In view of the imbalances in the indigenous production of long staple and short staple cottons during 1966-67, the availability of long and extra long staple cottons had to be supplemented by imports of such cottons to the extent of 7.8 lakh bales. The total consumption of cotton by the mills in that year amounted to 57.6 lakh bales. At the same time, the country could export 2.4 lakh bales of short staple Bengal Deshi Cotton, a non-spinnable export variety, which was not used by indigenous mills. As against this, in the 1979-80 season the country would meet the expected consumption requirements of the mills to the extent of 73 lakh bales dispensing with imports and discontinuing the policy of compulsory usage of man-made fibres in the manufacture of cotton textiles in February 1979. In addition, provison was made for exports of 6.55 lakh bales consisting of both short staple and long staple cottons, leaving a comfortable carry-over of about 24 lakh bales at the end of the season. Even in the worst drought year of 1979-80, cotton production was as high as 78.5 lakh bales. Therefore, unless there is a very bad crop year for cotton, the supply position in the country is expected to remain fairly comfortable in the years to come.

13. The table below gives the monthly index numbers of wholesale price of cotton and those of all commodities during the last five years :—

(*Base* : 1970-71 = 100)

Month	1975-76		1976-77		1977-78		1978-79		1979-80	
	All commodities	Cotton	All commodities	Cotton	All commodities	Cotton	All commodities	Cotton	All commodities (Provisional)	Cotton
September	178	135	180	201	188	190	187	168	221	165
October	177	130	178	206	185	182	188	167	222	166
November	171	126	177	207	184	177	188	168	220	167
December	168	129	177	202	185	185	185	167	224	167
January	166	139	179	214	184	186	186	165	224	162
February	165	141	183	215	181	179	185	162	228	164
March	162	138	183	209	183	178	189	164	230	166
April	166	152	184	210	182	175	196	167		
May	168	170	187	214	183	174	199	164		
June	173	185	188	210	185	174	202	162		
July	176	201	189	207	187	171	212	163		
August	178	197	188	198	187	168	218	162		
Average	171	154	183	208	185	178	195	165		

Source : Office of the Economic Adviser, Ministry of Industries, Government of India.

The index number of cotton prices, which in February 1977 was much higher than the general price index, now stands at a substantially lower level.

14. The major points made out before the Committee by the EICA, Bombay and other cotton associations from Gujarat, M.P. and Punjab and other

connected interests in favour of the resumption of futures trading in cotton were as follows :—

(i) The supply of cotton has improved substantially in recent years and that there was a large carry over at the end of the last two seasons. With more irrigated areas used for growing cotton in certain States and increased sowing of high yielding hybrid seeds and intensive cotton development programme in almost all cotton growing States the domestic crop is likely to increase further substantially in the coming years. Though consumption of cotton is also increasing, recent trends indicate that it is well below the internal production.

(ii) Cotton is harvested and marketed in the form of kapas in a short span of three to four months. After ginning, the full pressed bales of lint are sold to the mills throughout the year. The merchants and their associates have to carry substantial stocks of cotton till it is sold and have, therefore, to bear the risk of price fluctuations. They can buy from growers adequate quantities of cotton without discounting the prices to provide for such risk only if they have facilities to hedge.

(iii) The futures market protects ginners and pressers also, who buy kapas on their own account. They need this facility unt l they are able to dispose of cotton either for ready or for forward delivery.

(iv) Even after taking note of the operations of the CCI, the MSCMF and the growth of the co-operative movement, the private trade still markets about 60 per cent of the crop. This share of the trade may decline or increase, but so long as the trade is required to play a significant role in marketing of cotton, it will need the facility of hedging. The State as well as the co-operative agencies involved in the marketing of cotton could also use hedging facilities, to minimise their risks from adverse price fluctuations.

(v) Buffer stocks in cotton are costly and it is generally a losing operation. In the present conditions of cotton supply and demand and the inadequate warehousing facilities, such stocks of different varieties of cotton in adequate quantities cannot be built quickly enough. Moreover, the buffer stock agency itself may find futures markets useful for hedging its own stocks rather than holding them unhedged and assuming speculative risk.

15. The main arguments made out against the resumption of futures trading were as follows:—

(i) The Government is fixing support prices in respect of cotton and has also established the CCI, which carries out buying operations to ensure that the prices do not fall below economic levels.

(ii) Maintaining a buffer stock of cotton by the Government (as proposed in the Textiles Policy Statement of the Government announced on 7-8-1978), would have salutory impact on the cotton prices.

(iii) There is no need to permit futures trading in both kapas and cotton, when growers are concerned with the sale of kapas only.

16. The supply position of cotton in recent years has considerably improved as compared to the position in 1966, when futures trading was prohibited. The Agricultural Prices Commission, in its Report for 1979-80 submitted in April, 1979, has observed, "Both production and consumption of long staple cottons have been steadily rising. In the case of medium and short staples while production has been increasing, consumption has been on the decline. As a result, the country continues to be surplus in short staples and is moving towards self-sufficiency both in medium and long staple cottons." The conditions have improved further since then. There have been no imports during the last two years; exports of selected varieties have been permitted. Although the consumption of mills has been increasing, large stocks of cotton have to be carried forward by the functionaries in the trade. Despite the operations of the CCI, the MSCMF and the co-operative sector over a number of years, the cotton economy has remained a market oriented economy, as more than 50 per cent of the cotton is still marketed by the private trade, and the fluctuations in the prices of different varieties have remained quite large. It may also be mentioned that the A.P.C. in the above mentioned Report has pointed out that in one of the best crop years (i.e. 1978-79) the cotton prices showed a decline of more than 25 per cent in the case of certain varieties over those of the preceding year. These agencies also often sell their cotton to private trade when it suits them. Therefore, the demand of the private functionaries for hedging was permitted, it did impart some stability to dence to indicate that in the past when futures trading was permitted, it did impart some stability to prices (see Annexure VIII).

17. The argument was put forth by the Indian Cotton Mills Federation that the interest of the mills and the growers were identical and to increase production in cotton, the mills were offering better prices to growers than what the private traders could do under the facility of futures trading. The mills were not buying all the cotton directly from growers and the Federation could not substantiate its points by furnishing price data indicating that the prices paid by the mills to the farmers were generally higher than those paid by the traders.

18. It was brought to the notice of the Committee both by the trade and the Government Agencies that the mills refrained from purchasing cotton during the peak marketing periods which contributed to the sharp depression in prices. Therefore, the representatives of the MSCMF, who met us in Bombay, contended that they very much needed the facility of futures trading in cotton in view of the large stocks which the Federation had to handle thereby exposing themselves to a considerable risk involved in adverse

price fluctuations. In view of the emergence of a surplus situation, large fluctuations in prices, continued role of the private trade to a significant extent in the marketing of the commodity and the needs of the Public Agencies like the MSCMF, the Committee recommends that futures trading may be resumed in cotton at a few well selected centres.

19. The Committee also considered the issue whether futures trading was desirable in kapas or in cotton or in both. The marketing of kapas is seasonal as in that form it remains in the market only for about three to four months. Tradition of futures trading in kapas, moreover, is only in certain parts like Punjab and Saurashtra. The Committee, therefore, recommends that normally futures trading may be permitted in cotton but such trading may be permitted in kapas also at a few centres, where there has been long tradition of such trading and where functioning of competitive futures markets is possible.

III. Raw Jute and Jute Goods

(i) Raw Jute

20. Futures trading in raw jute has not been permitted since 1st September, 1964. Prior to that, such trading was conducted under the auspices of the East India Jute and Hessian Exchange Ltd., Calcutta, which is the only association granted recognition for the purpose. Trading in 'tsd and ntsd contracts in raw jute has been regulated through the said Exchange in the States of West Bengal, Bihar, Assam, Meghalaya, Orissa and Tripura and the Union Territories of Arunachal Pradesh and Mizoram. In the rest of the country, only ntsd contracts on a party to party basis can be entered into, as no association has been registered for the purpose.

21. The supply and demand position in raw jute since 1969-70 is given in the following table :—

(*Lakh bales of* 180 *kg each*)

Particulars	Season (July—June)										
	1969-70	1970-71	1971-72	1972-73	1973-74	1974-75	1975-76	1976-77	1977-78	1978-79	1979-80 Trade : estimates)
Supply											
I. Opening stocks :											
(*a*) With mills	3.56	9.80	10.50	12.50	8.00	22.00	14.00	7.60	6.00	4.30	
(*b*) With JCI	2.44	0.20	..	..	1.50	0.75	1.00	..	1.00	..	
(*c*) With other stockists ..	2.00	4.00	6.00	4.00	3.00	12.25	10.00	2.40	..	1.20	
Total carry over ..	8.00	14.00	16.50	16.50	12.50	35.00	25.00	10.00	7.00	5.50	27.00
II. Domestic Production :											
(*a*) Jute	56.55	49.38	56.84	49.78	62.20	44.71	44.40	53.53	53.61	64.54	
(*b*) Mesta	11.30	12.55	11.50	11.12	14.56	13.63	14.74	17.46	17.93	18.40	
Total ..	67.85	61.93	68.34	60.90	76.76	58.34	59.14	70.99	71.54	82.94	80.00
III. Imports	..	..	..	2.50	2.50	2.00	4.00	..	..	..	
Total supply ..	75.85	75.93	84.84	79.90	91.76	95.34	88.14	80.99	78.54	88.44	107.00
Disposal											
(*i*) Consumption :											
(*a*) By mills	62.00	63.50	74.50	69.00	62.50	63.00	75.00	68.00	68.00	62.30	77.00
(*b*) Domestic	2.00	2.00	2.00	2.00	3.00	3.00	2.00	2.50	2.50	3.00	3.00
(*ii*) Exports	2.00	1.00	3.50	0.50	2.00	4.00	1.00	0.50	..	..	
Total disposal ..	66.00	66.50	80.00	71.50	67.50	70.00	78.00	71.00	70.50	65.30	80.00
Calculated carry-over stocks ..	9.85	9.43	4.84	8.40	24.26	25.34	10.14	9.99	8.04	23.14	27.00
Estimated carry-over stocks ..	14.00	16.50	16.50	12.50	35.00	25.00	10.00	7.00	5.50	27.00	

Source—Production figures—Directorate of Economics & Statistics, Ministry of Agriculture and Irrigation, Government of India.
OTHER DATA—IJMA's monthly summary of Jute & Gunny Statistics.

The supply of raw jute (including mesta) has been large and sizeable stocks have generally to be carried forward from season to season. The carry-over at the end of 1978-79 and 1979-80 seasons was substantial under the impact of bumper crops, and lower mill consumption in 1978-79. The demand for jute is exclusively from jute mills for the manufacture of jute goods and the annual mill consumption is reckoned around 75 lakh bales. Exports have been negligible so far but may have to be allowed to support prices in view of the increased surplus.

22. Minimum support prices for raw jute introduced in 1962-63 are being fixed on a statutory basis from 1972-73. During 1969-70 to 1972-73 raw jute prices ruled well above the minimum prices. Thereafter they ruled generally at levels not significantly higher than the minimum prices excepting the period from May 1977 to July 1978 when they ruled substantially higher. In the 1979-80 season, raw jute prices were ruling mostly close to the minimum price levels of Rs. 200 per 100 kg. for West Bengal jute and Rs. 206 per 100 kg. for jute of other States for the W-5 grade in Calcutta. There were even reports of many transactions having taken place at less than the statutory minima both at Calcutta and upcountry centres.

23. Although the production of jute is spread over the eastern and northern parts of the country and in Andhra Pradesh, the consumption of jute is mainly concentrated in and around Calcutta where about 90 per cent of the total jute mills are located. This means that the jute produced at various centres in this region has to find an efficient and orderly marketing outlet till it reaches the final consumer viz., the jute mills. As the process of marketing is spread over the entire season, the commodity has to be held at difference stages by various functionaries. This is particularly important during the period of peak marketing. Excess arrivals lead to a fall in prices even to uneconomic levels adversely affecting the the interests of the growers. The Jute Corporation of India (JCI) established in 1971 operates in the market to provide price support particularly when the prices are prone to fall below economic levels. The operations of the JCI have, however, not succeeded in giving the required price support and its operations at best have never exceeded 10 per cent of the production. The purchases of the Corporation during the 1979-80 season have so far totalled only 8.48 lakh bales as against an estimated crop of about 80 lakh bales during the season.

24. Those who favoured futures trading in raw jute presented their case on the usual grounds that it would help the stockists and dealers to cover the risk of price fluctuations, the growers to get better prices and serve as an indicator of the future price trend. They also stated that the mechanism of futures trading would make the market more competitive and help in eliminating monopolistic tendencies. These who did not favour such trading were not sure that these benefits would flow from futures trading and felt that the existing facility of tsd contracts with the proposed plans to extend the scope of procurement scheme would meet the requirements.

25. Taking into account the supply and demand position in raw jute, the existing marketing arrangements and the views expressed by the various concerned interests, the Committee is of the view that futures trading in raw jute can play a useful role. The statutory minimum prices have not brought the required relief to the farmer. The operations of the JCI have also been of a small order to make any worthwhile impact. This indicates the need for supporting market mechanisms and futures trading can serve as a useful device to bring benefits to growers, stockists and other functionaries in the trade. The facilities of tsd and ntsd contracts serve the purpose of entering into long-term commitments and carrying adequate stocks safely if such facilities are coupled with futures trading facilities also. The Committee, therefore, recommends that futures trading in raw jute should be permitted.

(ii) **Jute Goods**

26. Among jute goods, futures trading is presently permitted only in sacking under the auspices of the East India Jute & Hessian Exchange Ltd., Calcutta, which is the only association recognised under the FC(R) Act for the purpose in the whole of India. Such trading in hessian is not being permitted since September 1971. Tsd and ntsd contracts in jute goods in the City of Calcutta can be entered into only under the said Exchange. In the rest of the country ntsd contracts on a party to party basis can be entered into whereas other types of farward contracts are prohibited.

27. The main items of production are hessian and sacking which generally form about 30 per cent and 49 per cent respectively of the total production of jute goods. The production of jute goods is spread over the entire year and the annual production is nearly 11 lakh tonnes. The trend in production and despatches of hessian and sacking may be seen from the following table :—

('000 tonnes)

Year (July—June)	Total production	Despatches: For internal purpose	Despatches: For export purpose	Despatches: Total	Year end stock	Total production	Despatches: For internal purpose	Despatches: For export purpose	Despatches: Total	Year end stocks
	HESSIAN					SACKING				
1969-70	341.4	64.7	239.6	304.3	58.2	377.3	310.8	55.2	366.0	36.7
1970-71	316.4	61.8	282.9	344.7	29.8	444.6	348.1	95.2	443.3	39.7
1971-72	331.0	64.8	274.8	339.6	21.6	498.8	376.3	130.7	507.0	34.6
1972-73	334.7	64.7	257.0	321.7	33.9	443.9	342.2	75.6	417.8	62.2
1973-74	295.7	65.5	229.7	295.2	34.4	376.1	285.6	110.5	396.1	42.8
1974-75	333.9	69.5	255.9	325.4	42.8	429.4	321.4	125.1	446.5	26.5
1975-76	282.7	76.0	213.5	289.5	37.4	620.0	525.1	61.0	586.1	58.9
1976-77	334.0	88.9	246.1	335.0	37.9	509.4	423.2	72.2	495.4	72.5
1977-78	346.1	89.2	270.5	359.7	24.5	444.2	402.2	73.7	475.9	38.4
1978-79	267.5	87.0	177.1	264.1	26.3	445.7	417.0	50.5	467.5	18.0
1979-80 .. .. (Upto March 1980)	265.4	64.0	179.5	243.5	50.4	426.8	376.1	40.8	416.9	27.1

Source—IJMA's Monthly Summary of Jute and Gunny Statistics.
Data pertain to mills reporting to IJMA.

28. Tsd contracts in hessian and sacking have been permitted all along as such contracts are used for ordinary non-speculative commercial transactions and more often than not, performed by issuing transferable delivery orders against which delivery of actual goods is given and taken. The jute mills need the facility of tsd contracts and they are also useful to the dealers who buy the goods from the mills for sale to the consumers. This type of contract is also useful to the exporters to obtain actual supplies of goods to meet the export requirements. Hence the tsd contracts are necessary for the smooth and orderly marketing of jute goods. Such contracts are, however, not a substitute for futures contracts as they cannot be used for the purpose of hedging.

29. Resumption of futures trading in hessian has been sought by the concerned interests, particularly the exporters, mainly on the grounds that it will protect the exporters from possible losses due to fluctuations in prices, facilitate immediate acceptance of global tenders as the export commitments can be hedged in the futures market, act as a barometer of prices on the basis of which export offers can be sent and thus promote exports. It will also break monopolistic tendencies by making the market competitive.

30. The facility of futures trading in sacking has been made use of by the dealers who sell to the domestic consumers including the DGS&D and other State agencies and the shippers who sell to the overseas buyers. The bulk of the outstanding purchases in the sacking hedge market are held against actual export commitments and sales to the DGS&D. The hedge market is also used for hedging stocks of jute goods and pucca delivery orders (Pdos). Although, the commodity is mainly consumed within the country, the futures market is helping the dealers to buy regularly from the mills and sell to the consumers. In fact a number of mills individually indicated that they find it easier to sell their goods to the dealers and the exporters when there is a facility of futures trading. The sacking futures market has functioned satisfactorily. The Committee, therefore, recommends its continuance.

31. As regards hessian, a substantial part of export business is handled by specialised export houses other than mills. Immediately after the conclusion of an export deal, it is not possible for the exporters to get the required goods through a tsd contract, since the construction or the quantum required by the exporter may not be readily available. This makes it necessary for the exporters to cover their export commitments in a futures market simultaneously with the export sale. In the absence of futures trading facilities, the exporters are very much handicapped and this has often resulted in the loss of export business and in some cases export markets. Hedging facilities would increase the competitive capacity of the exporters against the severe competition from other jute goods producing countries as also from synthetic substitutes by providing them protection against unfavourable price fluctuations. Further, the prices quoted in the futures market will be competitive and this would help to reduce monopolistic tendencies in the internal market and tone up its functioning. The Committee, therefore, recommends that futures trading in hessian should be permitted.

32. As regards carpet backing, the commodity is produced by the mills as per the specifications of the

foreign buyers and supplied to them directly. There is no domestic market in it and there has not been any demand for futures trading. The Committee, therefore, does not consider it necessary to permit futures trading in carpet backing for the present.

IV. Edible Oilseeds and Oils

33. The major edible oilseeds and oils produced in the country are (i) groundnut and groundnut oil, (ii) rapesead/mustardseed and its oil, (iii) cottonseed and cottonseed oil, (iv) sesamumseed and sesamum oil, (v) kardiseed and kardi oil and (vi) coconut oil. Regulated futures trading was permitted in groundnut and groundnut oil, rapeseed/mustardseed cottonseed and coconut oil. However, such trading has not been permitted in rapeseed/mustardseed from June 1964, groundnut and groundnut oil from October 1965 and cottonseed and coconut oil from October 1971. In the case of mustard oil, cottonseed oil, sesamumseed and sesamum oil and kardiseed and kardi oil regulated futures trading was never permitted.

34. Although India is one of the major oilseeds producing countries in the world, the total available supplies of all edible oilseeds and oils have generally fallen short of the domestic requirements. The trend in the supply of and demand for edible oilseeds and oils during the last few years is given in the following table :—

('000 tonnes)

Particulars	Season (November—October)													
	1973-74		1974-75		1975-76		1976-77		1977-78		1978-79		1979-80@	
	Seed	Oil	Seed	Oil	Seed	Oil	Seed	Oil	Seed	Oil	Seed	Oil	Seed	Oil
I. *SUPPLY*														
A. Indigenous Production														
1. Groundnut ..	4,152	1,345	3,578	1,157	4,728	1,516	3,699	1,192	4,261	1,400	4,471	1,470	4,000	1,327
2. Cottonseed ..	2,146	175	2,439	200	2,026	175	1,987	186	2,483	230	2,714	250	2,600	250
3. Mustardseed ..	1,704	545	2,252	715	1,936	616	1,551	479	1,650	500	1,877	570	1,600	486
4. Sesamumseed ..	485	150	392	119	479	136	422	161	520	160	540	170	370	132
5. Safflower (Kardiseed) ..	191	76	212	85	238	84	220	80	188	40	216	45	250	91
6. Coconut oil ..	..	173	...	178	..	181	..	170	..	169	..	169	..	169
7. Others* ..	..	139	..	174	..	166	..	139	..	120	..	120	..	120
Total availability ..		2,603		2,628		2,874		2,407		2,619		2,794		2,575
II. *DEMAND*														
A. Consumption by Vanaspati units ..	..	414	..	446	..	568	..	621	..	676	..	679	..	680 (P)
B. Exports	..	..	..	1	..	11	..	3	..	1	..	Neg.	..	Neg.
C. Household consumption	Estimates not available									2,739 £	..	2,852 £	..	2,968 £
Total demand ..	Not worked out									3,416	..	3,531	..	3,648
III. *GAP*	Not worked out									(—)797		(—)737		(—)1,073
IV. *IMPORTS* ..		155		52		17		907		1,167		1,100 (P)		1,000 (P)

Source—(*a*) Oilseeds and Oils Production—Economics and Statistical Advisor, Ministry of Agriculture and Irrigation, Government of India.

(*b*) Consumption by vanaspati units—Directorate of Vanaspati, Government of India.

(*c*) Imports and Exports—Bombay Oilseeds and Oils Exchange Ltd., Bombay.

*These include (*i*) Soyabean oil, (*ii*) Sunflower oil, (*iii*) Nigerseed oil and (*iv*) 20 per cent of total production of linseed oil used for edible purposes.

@Production as estimated by trade.

£ Estimates of Study Group, constituted by the Ministry of Commerce, Civil Supplies and Co-operation, Govt. of India, on "A Long-term Edible Oils Plan" made in August 1978.

(P) Provisional.

(Neg.)—Negligible.

The point that emerges from the above table is that the annual production of edible oils in the country has remained generally stagnant around 27 lakh tonnes. On the other hand, the annual demand of households and vanaspati factories for edible oils is rising year after year with the increase in population and the improvement in the general standard of living and has been reckoned at about 35 lakh tonnes during 1978-79. The shortfall in supplies is being made good largely by imports which were as high as

11.6 lakh tonnes in 1977-78. The gap in demand and supply has been estimated by Study Group at 7.37 lakh tonnes for 1978-79. This gap, as estimated by some private sources, is as high as 15-16 lakh tonnes for 1979-80. In any case, the gap is effected to widen in the absence of the required break-through in the production of edible oilseeds within the country. The projections of supply and demand for edible oils in the country during the period 1980-81 to 1989-90 given in the following table bring out this point.

Projections of Supply of and Demand for Edible Oils

(*lakh tonnes*)

Particulars	1980-81	1983-84	1986-87	1989-90
I. *SUPPLY*				
1. Groundnut oil	15.39	17.24	19.31	21.62
2. Cottonseed oil	2.90	3.80	4.70	5.60
3. Mustard oil	6.91	7.43	7.98	8.59
4. Sesame oil	1.52	1.57	1.63	1.69
5. Safflowerseed oil (Kardi oil)	0.53	0.65	0.80	0.98
6. Coconut oil	2.04	2.33	2.67	3.05
7. Others	1.92	2.80	3.17	3.60
II. Total supply	31.21	35.82	40.26	45.13
III. Total demand	38.05	43.22	48.98	55.42
IV. Gap	6.84	7.40	8.72	10.29

Source—Report of the Study Group on "A Long-Term Edible Oils Plan".

35. The persistent imbalance in the supply of and demand for edible oilseeds and oils in the country has led to a generally rising trend in their prices. The price behaviour, however, indicates that despite the steady rise over the years, there has generally been post-harvest fall and lean period rise within a season in the case of most of the edible oilseeds and oils. Edible oils, being an item of mas consumption, the Government have sought to keep their prices at reasonable levels by imports and protect consumer by regular releases of such oils through the public distribution system.

36. The representatives of the trade and other concerned interests who met the Committee pleaded for the resumption of futures trading in groundnut and groundnut oil, rapeseed/mustardseed, cottonseed and coconut oil. They also pleaded for introducing futures trading in soyabean, the production of which has been rising steadily in recent years. The main reasons mentioned in support of such resumption were that it would facilitate orderly marketing of these commodities, reduce intra-seasonal fluctuations in prices and serve as an indicator of the future price trend. It was also mentioned that there has been a long tradition of futures trading in these commodities and such trading was successfully regulated under the FC(R) Act. They did not press for futures trading facilities in other edible oilseeds and oils like sesamumseed, kardiseed and their oils where there has been no tradition of such trading.

37. The Committee has weighed the pros and cons of permitting futures trading in the edible oilseeds and oils mentioned above. Although the total production of major edible oilseeds and oils is large in absolute terms, a serious secular shortage of these commodities in relation to the demand has emerged in this country. This has resulted in large, violent and frequent fluctuations in the prices of major oilseeds and oils. Under these circumstances, in our opinion, edible oilseeds and oils are not, in the present stage, commodities fit for being permitted for futures trading as it is not clear whether social gains through futures trading will be larger than private gains. The Committee, therefore, recommends that futures trading in edible oilseeds and oils should not be permitted for the present.

38. While, on balance, this Committee does not consider the edible oils and the commodities from which these edible oils are derived as a fit subject for futures trading in the current phase, it has noticed the great variation and violent fluctuations in the prices of these items in the 1960s and 1970s. These commodities are of wide public consumption and are consumed by the rich and poor alike. It is extremely important in the opinion of this Committee to augment the supplies and to reduce the fluctuations in availability and indeed to restrain demand to the extent possible.

39. The Committee notes that the primary cause of restricted supplies in relation to high demand is the absence of any major break-through in the production technology of these commodities. It is, therefore, to be recommended that large resources, e.g. research and development, should be devoted to edible oilseeds so that at an early date supplies are substantially augmented through internal production as was done in the context of the 'green revolution' in wheat and one or two other commodities. Until this happens, the Committee further suggests that the regulatory mechanism already in operation should be continued and further strengthened. This will perhaps include input supplies to farmers, propagation of new technology, a support price, a procurement price and procurement operation, a buffer stock operation, a public distribution system of fair price shops and other suitable machinery. Only when supply is augmented, an important condition for the operation of futures market might emerge in these commodities in future.

V. Castorseed

40. Futures trading in castorseed was conducted under the auspices of associations recognised under the FC(R) Act at Bombay and Ahmedabad since 1955. Prior to this, such trading was conducted at Bombay under the Bombay Forward Contracts Control Act but it was carried on freely at a number of other centres in the rest of the country. Futures trading as well as other types of forward trading in castorseed was banned in February 1977. However, futures trading in castor oil was banned as early as in January 1955, and has remained so as traders including exporters preferred castorseed as a medium for hedging their commitments both in castorseed and castor oil

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due to long tradition of such trading in castorseed and larger supply of castorseed than that of caster oil. The ban on farward trading in castorseed on 5-2-1977 was imposed along with the ban on exports of castor oil in view of continuously rising prices of oilseeds and oils. Although the ban on exports of castor oil was lifted in May 1977, the ban on forward trading in castorseed has continued.

41. The supply of and demand for castorseed and castor oil from 1968-69 are given in the following table :—

('000 tonnes)

Particulars	Season (November—October)										
	1968-69	1969-70	1970-71	1971-72	1972-73	1973-74	1974-75	1975-76	1976-77	1977-78	1978-79
I. *SUPPLY*											
(*i*) Production	116.00	123.00	136.00	154.00	145.00	229.00	210.00	143.00	179.00	217.20	236.00
(*ii*) Retained for seeding purpose @ 6%	6.96	7.38	8.16	9.25	8.70	13.70	12.60	8.58	10.74	13.03	14.16
(*iii*) Total marketable surplus for crushing.											
(*a*) In terms of seed ..	109.04	115.62	127.84	144.75	136.30	215.30	197.40	134.42	168.26	204.17	221.84
(*b*) In terms of oil ..	43.62	46.25	51.14	57.90	54.52	86.12	78.96	53.78	65.90	81.67	88.74
(*iv*) Carry over from the previous season	N.E.	4.12	6.57	18.51	22.51	0.03	23.65	48.81	13.59	12.69	10.36
Total availability in terms of oil (*iii*) (*b*) + (*iv*)	43.62	50.37	57.71	76.41	77.03	86.15	102.61	102.59	80.49	94.36	99.10
II. *DEMAND IN TERMS OF OIL*											
(*i*) Exports	14.50	18.80	14.20	28.90	52.00	32.50	23.80	54.00	32.80	44.00	47.00
(*ii*) Domestic use	25.00	25.00	25.00	25.00	25.00	30.00	30.00	35.00	35.00	40.00	40.00
TOTAL ..	39.50	43.80	39.20	53.90	77.00	62.50	53.80	89.00	67.80	84.00	87.00
Carry-over stocks ..	4.12	6.57	18.51	22.51	0.03	23.65	48.81	13.59	12.69	10.36	12.10

Source—(*i*) Figures of production are from Directorate of Economics and Statistics, Ministry of Agriculture and Irrigation, Government of India.

(*ii*) The percentage share retained for seeding purposes is as reckoned by Ministry of Agriculture, Government of India.

(*iii*) Figures of exports are from (*a*) Monthly Statistics of Foreign Trade of India upto 1974-75 and (*b*) The State Trading Corporation of India from 1975-76 onwards.

(*iv*) Figures for domestic use are collected from (*a*) The Central Organisation for Oil Industry and Trade and (*b*) Hindustan Lever Ltd.

N.E.—Not estimated.

42. The supply and demand position indicates that even after meeting the domestic requirement, large surpluses are available for exports. Large stocks of castorseed and castor oil have to be held by the crushers, stockists and exporters both for domestic consumption and exports.

43. Although exports of castor oil are canalised through the State Trading Corporation (STC) since September 1971, the private trade is actively associated with exports of castor oil. The STC generally enters into firm contracts with foreign buyers at an agreed price and thereafter enters into purchase contracts with its associates, where under the oil is made available to it at the time of shipments, normally three to four months from the date of the contract.

44. One of the reasons reported for banning futures trading in castorseed was that such trading had a bullish impact on the groundnut oil prices. It was observed that even after the ban on futures trading in castorseed, the prices of groundnut oil continued to rise. The ready prices of castorseed/castor oil also ruled generally firm during the period subsequent to the ban till the end of October, 1977. In the following 1977-78 season, the ready prices of castorseed/castor oil showed a declining trend whereas those of groundnut oil continued to rule at higher levels. The price behaviour indicates that there is no direct relationship between the prices of castorseed/castor oil and those of groundnut oil and that the ban had not helped in exercising a stabilising influence on the prices of the latter. This is mainly because the total annual production of castor oil a non-edible commodity as distinct from groundnut oil, forms only an insignificant proportion of the total production of groundnut oil and hence the prices of castorseed and its oil cannot have any determining influence on the prices of groundnut oil.

45. The representatives of the trade and other interests pleaded for the resumption of futures trading in castorseed, mainly on the following grounds. The commodity was in surplus after meeting internal requirements and a sizeable quantum was available

for export. The traders/crushers, who supplied castor oil to the STC had to assume the risk arising from price fluctuations, in the absence of the facility of futures trading either in castorseed or castor oil. A crusher, when he sold oil on forward basis to the STC, quite often did not possess adequate stocks of seeds to cover such sales. If there were a futures market, a crusher could, about the time of his forward sale of oil to the STC, purchase a corresponding quantum on the castorseed futures market. The STC, which is the canalising agency for exports of castor oil, also pleaded with the Committee that resumption of futures trading in castorseed would be helpful to promote exports of castor oil.

46. The Committee has carefully considered the views expressed by the various concerned interests. Being export oriented with about 50 per cent of castor oil produced finding an outlet to the overseas markets, the prices of both castorseed and castor oil are determined to a great extent by the developments taking place in the international markets. Taking into consideration this important aspect as also the pleadings made by various concerned interests including the STC, the Committee recommends that futures trading in castorseed should be resumed.

47. The Committee has considered whether futures trading in castor oil is also necessary. Although it is castor oil that is exported, the facility of futures trading has been sought by all the concerned interests only in castorseed. Besides, the market for castor oil is quite narrow. It may also be pointed out that futures trading in this country has been conducted only in castorseed. Further, the need for hedging in castor oil can be met through the facility of futures trading in castorseed. The Committee, therefore, recommends that there is no need to introduce futures trading in castor oil.

VI. Linseed

48. Futures trading as well as other types of forward trading in linseed have been banned since 5th February, 1977. Futures trading in linseed till than was conducted under the auspices of the associations recognised under the FC(R) Act at Bombay, Kanpur and Gwalior. Futures trading in linseed oil, however, was banned as early as in January 1955 and has remained so since then. The ban on forward trading in linseed on 5-2-1977 was imposed along with the ban on exports of linseed oil in view of the continuous rise in the prices of edible oilseeds and oils and this ban continues.

49. The supply of and demand for linseed and linseed oil from 1968-69 are given in the following table :—

('000 tonnes)

Particulars	Season (April—March)										
	1968-69	1969-70	1970-71	1971-72	1972-73	1973-74	1974-75	1975-76	1976-77	1977-78	1978-79
I. *SUPPLY*											
(*i*) Production	329.00	469.00	474.00	529.00	428.00	504.00	564.00	598.00	419.00	527.00	514.00
(*ii*) Retained for seeding purpose @ 5%	16.45	23.45	23.70	26.45	21.40	25.20	28.20	29.90	20.95	26.35	25.70
(*iii*) Direct consumption of seed @ 6%	19.74	28.14	28.44	31.74	25.68	30.24	33.84	35.88	25.14	31.62	30.84
(*iv*) Total marketable surplus											
(*a*) In terms of seed ..	292.81	417.41	421.86	470.81	380.92	448.56	501.96	532.22	372.91	469.03	457.46
(*b*) In terms of oil@33% of (*a*)	96.63	137.75	139.21	155.37	125.70	148.02	165.65	175.63	123.06	154.78	150.96
(*v*) Carry-over from the previous season	18.00	0.81	10.35	10.84	21.83	8.51	2.23	Nil	2.35	2.35	12.96
Total availability in terms of oil [(*iv*)(*b*)+(*v*)]	114.63	138.56	149.56	166.21	147.53	156.53	167.88	175.63	125.41	157.13	163.92
II. *DEMAND IN TERMS OF OIL*											
(*i*) Exports	0.002	0.004	0.002	..	0.02	17.50	20.36	51.62	1.57	..	..
(*ii*) Paint industry	70.00	70.00	80.00	80.00	80.00	70.00	70.00	70.00	70.00	70.00	70.00
(*iii*) Soap industry	10.00	10.00	10.00	10.00	15.00	15.00	20.00	20.00	20.00	20.00	20.00
(*iv*) Edible use*	33.82	48.21	48.72	54.38	44.00	51.80	57.52	31.66	31.49	54.17	52.84
TOTAL ..	113.82	128.21	138.72	144.38	139.02	154.30	167.88	173.28	123.06	144.17	142.84
Carry-over at the end of the year	0.81	10.35	10.84	21.83	8.51	2.23	Nil	2.35	2.35	12.96	21.08

Source—Production—Directorate of Economics & Statistics, Ministry of Agriculture and Irrigation, Government of India.
Exports—Monthly Statistics of Foreign Trade of India.
Industrial demand—Central Organisation for Oil Industry and Trade.
*Edible use including for adulteration—35 per cent of I(*iv*) (*b*) or the 'residual' of supply, whichever is lower.

The production of linseed and linseed oil has recorded a substantial rise. The paint industry is the largest user of linseed oil and the soap industry's consumption of the oil also has doubled. The use of linseed oil for edible purposes (including adulteration) has risen notably in recent years. Exports of linseed oil rose sharply in 1975-76 but have been banned since 5-2-1977.

50. The price trends in edible oilseeds and oils reveal that even after the ban on futures trading in linseed, the prices of these items continued to rule firm till the close of the 1976-77 season and remained at fairly high levels during the 1977-78 season. In the case of linseed, the ready prices rose to record levels in September 1977 even after the ban. Thus the ban on futures trading in linseed did not arrest the rising trend in the prices of linseed and linseed oil and of edible oilseeds and oils.

51. A section of the trade opposed futures trading on the following grounds. Linseed oil is being increasingly used as edible oil in some parts of the country, as well as for blending and/or adulteration with other edible oils particulary mustard oil in view of the shortage of supplies of edible oils in the country. Secondly, India was not importing cheaper non-edible oils for industrial purposes and hence it was not desirable to permit the exports of linseed oil. If the export of linseed oil were not permitted the need for futures trading in linseed would get reduced.

52. Those who supported futures trading advanced the following reasons: Futures trading in linseed generally produced a sobering influence on its ready prices. The prices of linseed did not have a direct bearing on the prices of edible oilseeds and oils. The entire marketing of linseed and linseed oil was done by the private trade and hence the facility of hedging and forecasting the future trend of prices was essential to the trade.

53. The Committee has considered the question of permitting futures trading in linseed in the light of the supply and demand situation in the commodity and the views expressed by the concerned interests. The rise in the production of linseed, emergence of sizeable carry over stocks in recent years, and the absence of any direct relationship between the prices of linseed oil and edible oils are points in support of futures trading in linseed. Further, since as much as about the two thirds of the production linseed oil is used for non-edible purposes viz., industrial use, the argument that futures trading in linseed should not be permitted because linseed oil is used for edible purposes does not carry sufficient conviction. We also note that futures trading in linseed had been permitted uninterruptedly for about 20 years till it was banned in February 1977. Until then futures trading in this commodity had functioned satisfactorily. We, therefore, recommend that futures trading should be permitted in linseed.

54. On the question as to whether futures trading is necessary in linseed oil, the points to be noted are that exports of linseed oil are presently banned and there has neither been any tradition of futures trading in linseed oil nor any demand for such trading from the concerned interests. Moreover, the market for linseed oil is quite narrow. Hence we do not consider it necessary to permit futures trading in linseed oil.

VII. **Oilcakes**

55. The oilcake-group consists of a number of different oilcakes and the supply and demand situation in each varies considerably. Oilcakes may be broadly grouped into major and minor oilcakes. Major oilcakes are groundnut oilcake, cotttonseed oilcake, rapeseed/mustardseed oilcake, linseed oilcake and sesamum oilcake. Oilcakes such as mahua oilcake, sal oilcake, neem oilcake, etc., which are obtained mostly from oilseeds of tree origin are considered as minor oilcakes. Oilcake is a by-product obtained in the process of crushing oilseeds for the extraction of their oils. The oilcake thus obtained is called *expeller cake,* which normally contains six to seven per cent oil. This expeller cake can then be subjected to a solvent extraction process for extracting the remaining oil and the cake obtained in the process is called *extraction cake* or deoiled meal. In some cases like rice bran, oil is obtained directly by extraction process and there is no intermediate stage of expeller cake.

56. Futures trading is not permitted at present in any of the expeller or extraction cakes. Such trading was, however, regulated in groundnut expeller cake from March 1963 to May 1964. It was banned from June 1964 in view of the rising prices of groundnut and groundnut oil and its impact on the prices of cake. Futures trading in the cakes of rapeseed/mustardseed, sesamum, taramira and cottonseed was banned in June, 1964 in view of the reports that the names of these cakes were used for conducting futures trading in the prohibited commodities like gram, peas, ground-

nut, groundnut oil etc.[1] Futures trading in linseed oilcake was banned in June 1979 for the same reason. However, ntsd contracts in groundnut oilcake (both expeller and extraction) are permitted under a registered association viz., The Solvent Extractors Association of India, while in other oilcakes such contracts are banned with suitable exemptions to genuine functionaries. In the case of minor oilcakes, futures trading cannot be organised as no association has been registered under the FC(R) Act for the purpose.

57. The trends in production of major oilcakes and exports of their extractions are given in the following table :—

('000 tonnes)

Particulars	November—October					
	1974-75	1975-76	1976-77	1977-78	1978-79	Percentage to total (item 7) in 1978-79
1. *Groundnut Oilcake*						
(*a*) Production						
(*i*) Expeller	1,736	2,274	1,789	2,121	2,235	41.8
(*ii*) Extraction	1,614	2,115	1,664	1,973	2,079	37.6
(*b*) Exports* .. .. (Extraction)	612	599	1,234	541	523	42.0
2. *Cottonseed Oilcake*						
(*a*) Production						
(*i*) Expeller	1,011	1,015	N.A.	1,172	1,311	24.5
(*ii*) Extraction	940	944	..	1,090	1,219	22.0
(*b*) Exports* .. .. (Extraction	123	155	103	162	215	17.3
3. *Rapeseed Oilcake*						
(*a*) Production						
(*i*) Expeller	1,431	1,232	972	1,016	1,179	22.1
(*ii*) Extraction	1,331	1,146	904	945	1,090	19.7
(*b*) Exports* .. .. (Extraction)	..	..	..	40	60	4.8
4. *Linseed Oilcake*						
(*a*) Production						
(*i*) Expeller	339	361	247	301	307	5.7
(*ii*) Extraction	315	336	230	280	286	5.2
(*b*) Exports* .. .. (Extraction)	46	74	121	44	..	..
5. *Sesame Oilcake*						
(*a*) Production						
(*i*) Expeller	178	205	242	279	310	5.9
(*ii*) Extraction	166	191	225	259	288	5.2
(*b*) Exports* .. .. (Extraction)	5	7	6	14	..	..
6. *Deoiled Rice Bran*						
(*a*) Production						
(*i*) Expeller	..	..	..	..	..	..
(*ii*) Extraction	137	230	465	481	574	10.3
(*b*) Exports* .. .. (Extraction)	102	203	402	309	446	35.9
7. *Total*						
(*a*) Production						
(*i*) Expeller	4,695	5,087	3,250	4,889	5,342	..
(*ii*) Extraction	4,503	4,962	3,488	5,028	5,536	..
(*b*) Exports*	888	1,038	1,866	1,110	1,244	..

SOURCE : *Production of Expeller Oilcake*—Oilseeds Situation in India issued by Economic and Statistical Adviser, Ministry of Agriculture and Irrigation, Government of India.
Production of Cottonseed Expeller Oilcake—All India Cottonseed Crushers' Association.
Production of Extraction Cakes—Estimated on the basis that, on an average, 7% of the oil on the weight of the expellercake can be extracted out. (Findings of Regional Research Laboratory, Hyderabad).
Exports—Monthly Statistics of the Foreign Trade of India, issued by the Directorate and General and Commercial Intelligence and Statistics, Calcutta and Oilseeds Situation in India.
*Export figures are for the period April to March.
Production of Deoiled Rice Bran and Export—The Solvent Extractors' Association of India.
[1]Forward Markets Commission's Annual Report, 1964—pages 13 and 23

58. Groundnut oilcake has the predominant position both in respect of production and exports of extractions accounting for about 42 per cent and about 66 per cent of the total production and exports respectively. Exports of groundnut expellor cakes were banned from April 1963. Since then, exports of all other expeller oilcakes have also been banned with a view to encouraging the extraction of the oil content in the expeller oilcakes and to promote the exports of extraction cake, which only at present are permitted. There are 220 solvtnt extraction plants in the country which are engaged in the extraction of oil and most of these plants also export extraction cakes. A small proportion of the export extraction is also undertaken by private exporters.

59. No authoritative data regarding the production of minor oilcakes are available. The estimates of such production based on the availability of minor oilseeds as given in the Report (1971) of the Committee appointed by the Ministry of Food and Agriculture, Government of India, are given in the following table :

Commodity	Seed (Tonnes)	Oil yield %	Oil (Tonnes)	Oilcakes (Tonnes)
1. Mahua ..	71,428	35	25,000	45,500
2. Neem ..	100,000	20	20,000	80,000
3. Karanj ..	25,900	27	7,000	18,000
4. Kusum ..	9,000	33	3,000	6,000
5. Sal ..	25,000	12.5	3,125	21,000
6. Kokum ..	500	40	200	300
7. Others .. (khakan, undi, etc.)	1,687	46.5	675	1,000
Total ..	233,515		59,000	1,71,800

No significant change in the availability of minor oilseeds seems to have taken place as the trade has been reporting more or less the same figures in respect of these minor seeds and cakes since then.

60. In the case of minor oilcakes, not only their production is quite small but also there is no assured supply of even a minimum quantity. For instance, the production of Mahua cake, which worked out to about 45 thousand tonnes in 1978, was between 13 to 16 thousand tonnes only in 1979,[1] on the basis of the availability of the seed. Even in a normal year, the production of Mahua cake may vary between 26 to 35 thousand tonnes. Unremunerative price paid to the tribal collectors is one of the reasons for low collection of these seeds. The other reasons are the absence of the necessary infrastructure and organised ready markets for the seeds. The present collection is mainly from areas which are easily accessible. Collection from interior forests has not been possible due to the absence of roads and difficulties of collection in the rainy season. Lack of storage in the interior forest areas is another handicap. Contractors who are moinly responsible for the collection of seeds are not interested in developing necessary infrastructure being not sure of getting the lease of allotted areas for collection continuously. The supply of their oils is also irregular as the crushers generally undertake crushing of such seeds only when they do not have stocks of major oilseeds like groundnutseed or mustardseed. In view of the extremely small size and unorganised nature of the markets in minor oilseeds, this Committee considers that there is no case for permitting futures trading in any of the minor oilcakes at present. A view was, however, expressed by one of the members of the Committee that futures trading in mahua oilcake to the extent it influences spot prices of the mahuaseed might ensure better prices for mahuaseed and may enlarge the collection of the seeds thereby benefiting the collectors.

61. Some of the crushers of groundnut requested for the facility of futures trading in expeller oilcake, although it was not favoured by the solvent extraction industry which is the main consumer of expeller oilcake and exporter of solvent extractions. The STC has favoured futures trading in solvent extractions on the ground that it would facilitate exports of extractions. However, the Solvent Extractors Association has not pressed for such a facility.

62. The Committee has looked at the whole question primarily from the point of view of promoting exports of extractions. It has noted that the expeller oilcake contains six to seven per cent oil and it is in the interest of not only the domestic consumers of edible oils but also of the extraction industry that this oil is extracted within the country itself. The Government of India have already banned the exports of all expeller oilcakes. Further, as stated earlier, futures trading in the groundnut expeller oilcake, which in terms of production accounts for the bulk of total production of expeller cakes, was banned due to rising prices of the groundnut group of commodities. This situation continues. In respect of other expeller oilcakes like rapeseed cake, linseed cake, etc., such trading was banned because of their misuse for trading in banned commodities. In view of the position as aforesaid we consider that there is no need for permitting futures trading in expeller oilcakes for the present.

63. As regards extractions, the supply is quite large, the demand for it, which is mainly from the overseas buyers, is uncertain and the international market for it is highly competitive. The quantum of exports of extraction is sizeable. The commodity is also suitable for futures trading. Although the solvent extractors have not presently demanded the facility

[1]The information supplied by the Hindustan Lever Ltd., in November 1979 was as follows : —"Our experience shows that the actual availability of seeds (mahua) varies between 40,000 to 55,000 tonnes per annum in an average year. The oil yield of the seeds is 38% to 40%. Therefore, in an average year, 16,000 to 20,000 tonnes of oil is obtained through the expeller or extraction processes. 1978, however, was a very good year when the availability of seeds was estimated at 70,000 tonnes. 1979 has been an extremely poor year with the availability of seeds estimated at 20,000 to 25,000 tonnes." Regarding neemseed, they have informed that its production was 40,000 tonnes in 1978 and 1,00,000 tonnes each in 1979 and 1980.

of futures trading in extractions, properly organised futures markets in major extraction cakes would be useful for promoting their exports and hence in the long term interest of the country. Since on the basis of production and exports, groundnut extractions have been found to be eminently suitable for being traded on a futures market, the Committee recommends that initially this facility may be extended in respect of groundnut extractions and extended to other major extractions such as rice bran de-oiled cake. However, the actual opening of futures markets should follow the coming into existence of a representative association at a suitable centre.

VIII. Pepper

64. Futures trading in pepper is conducted at Cochin and Bombay. Regulated futures trading in pepper at Cochin is conducted under the India Pepper & Spice Trade Association since January 1957. Such trading in Bombay under the Pepper and Ginger Merchants Association is being conducted since February 1963.

65. The production and exports of pepper since 1968-69 are given in the following table :—

Season (November-October)	Production (,000 tones)		Exports (tonnes)
	Official estimates	Trade estimates	
1968-69	26	35	19,482
1969-70	25	30	19,787
1970-71 . ..	26	28	18,670
1971-72	26	33	20,000
1972-73	26	36	25,000
1973-74 . ..	29	35	25,327
1974-75	28	38	26,000
1975-76	29	32	19,300
1976-77	34	38	25,000
1977-78	34	36	20,780
1978-79 . ..	34 (Final)	36	18,337

Source—Official estimates from the Directorate of Economics & Statistics, Ministry of Agriculture and Irrigation, Government of India.
Trade estimates from India Pepper and Spice Trade Association, Cochin.
Exports from Pepper and Ginger Merchants Association, Bombay.

The production of pepper in recent years has remained steady around 35-36 thousand tonnes. The exports, which showed a more or less steady rise from 1968-69 till 1974-75, are in recent years fluctuating with a generally downward trend. Pepper being primarily an export commodity, its prices are influenced largely by international factors such as production trends and exports from competing countries like Indonesia, Sarawak, Malaysia, Sri Lanka, Brazil and Madagaskar, demand from importing countries and price trends in the international markets.

66. The representatives of various concerned interests in the commodity pleaded for the continuation of futures trading. In the absence of a futures market the exporters would be exposed to undue price fluctuations.

67. The supply of pepper during a season is fairly large. Out of an annual production of about 35 thousand tonnes, the domestic consumption forms only about one-third and the rest is available for export. The demand for the commodity emanating from overseas buyers is particularly susceptible to wide variation causing undue price fluctuations. This causes hardships to the producers, stockists and exporters. The facility of futures trading in pepper is extensively used by exporters and stockists. During 1977-78, about 65 per cent of the purchase position and 53 per cent of the sale position in the pepper futures market at Cochin were held as hedge against actual export commitments and stocks. Taking into account all these factors, the Committee recommends that futures trading in pepper should be continued.

IX. Turmeric

68. Futures trading in turmeric is being regulated under the FC(R) Act since April 1956 under the auspices of the Spices and Oilseeds Exchange Ltd., Sangli, which is the only association recognised for such trading in the whole country.

69. The supply and demand position in turmeric from 1968-69 to 1979-80 is shown in the following table :

('000 tonnes)

Season (December—November)	Opening Stocks	Production (Marketable surplus)	Total availability (2 + 3)	Exports	Internal consumption (4—5+7)	End-season stocks
1	2	3	4	5	6	7
1968-69	1.0	93.0	94.0	6.4	86.6	1.0
1969-70	1.0	106.0	107.0	7.0	95.0	5.0
1970-71	5.0	152.0	157.0	11.1	130.9	15.0
1971-72	15.0	89.0	104.0	14.2	62.8	27.0
1972-73	27.0	77.0	104 0	6.7	82 3	15.0
1973-74	15 0	101.0	116.0	7.9	85.1	23.0
1974-75	23.0	100.0	123.0	9.2	103.8	10.0
1975-76	10.0	102.0	112.0	11.8	75.2	25.0
1976-77	25 0	84.0	109.0	11.8	87.2	10.0
1977-78	10.0	107.0	117.0	9.3	104 7	3.0
1978-79	3.0	164.0	167.0	20.0	117.0	30.0
1979-80*	30.0	170.0	200.0	N.A.	N.A.	N.A.

Source : The Spices and Oilseeds Exchange Ltd., Sangli.
*Estimates as on 1-4-1980.
N.A. - Not available.

More than 90 per cent of the production of turmeric is consumed within the country while about 8 to 10 per cent is exported. In view of the inelastic nature of the demand for turmeric and limited exports, even a marginal increase or decrease in production brings about a significant decline or rise in its prices.

70. The supply and demand position in turmeric is such as to require the concerned marketing functionaries to carry large stocks of the commodity in the

process. They need hedging facilities to protect themselves against adverse price fluctuations which are inevitable in the commodity due to varying supply and inelastic demand. Further, there has been a long tradition of futures trading in the commodity. The various concerned interests have, therefore, pressed for the continuance of this facility for the orderly marketing of turmeric. Although exports of turmeric are somewhat limited, the exporters have also sought the continuance of the facility of hedging to cover the risk arising from price fluctuation and for promoting exports.

71. The experience of regulation of futures trading in turmeric has been satisfactory. Due to large variability in supply and inelastic demand the turmeric prices are susceptible to large fluctuations. Futures prices by serving as advance indicators have exercised, during periods of sharp fall or rise in the ready prices, a restraining influence on them. The dealers and exporters benefitted from the futures market in turmeric, the former by hedging their stocks and the latter by purchasing on the futures market against their actual export commitments. The Committee, therefore, recommends that the facility of futures trading in turmeric should be continued.

X. Sugar and Gur

72. No regulated futures trading has ever been permitted in sugar. In gur, however, such trading was permitted under the FC(R) Act from July 1959 to January 1963, from March 1970 to October 1971 and from December 1978 to March 1980.

73. The production of sugarcane, sugar, gur and khandsari and the proportion of sugarcane used in their manufacture are given in the following table :—

Season (October-September)	Production of sugarcane (lakh tonnes)	% of cane utilised for manufacture of sugar	Production of sugar (lakh tonnes)	% of sugar cane used for production of gur and khandsari	Production of gur and khandsari@ (lakh tonnes)
1966-67	9,28	23.3	21.51	64.8	61.25
1967-68	9,55	23.5	22.48	64.7	63.05
1968-69	12,47	32.0	35.59	56.0	66.69
1969-70	13,50	33.9	42.62	54.1	60.40
1970-71	1,264	30.2	37.40	57.8	74.37
1971-72	11,36	27.3	31.13	60.8	69.98
1972-73	12,49	32.4	38.73	55.6	70.30
1973-74	14,08	30.0	39.48	58.0	83.66
1974-75	14,43	33.6	47.97	54.5	80.63
1975-76	14,06	29.8	42.64	58.3	83.67
1976-77	15,30	32.0	48.40	56.1	88.41
1977-78	17,70	38.0	64.58	50.1	90.88
1978-79	15,65	38.2	58.58*	50.1	79.22

@About 15% of the gur and khandari production is normally taken to represent production of khandsari.

*Provisional.

Source : Sugar situation issued by the Economic and Statistical Advisor, Ministry of Agriculture and Irrigation, Government of India.

The production of sugar has shown sharp fluctuations. In view of large variations in the supply of sugar and the demand for it continuously rising, sugar has been subjected to control of one form or the other. The partial control policy adopted in 1967 whereunder the Government acquired about 60 to 70 per cent sugar as levy sugar for sale at fixed prices leaving the remaining 30 to 40 per cent sugar for free market has been continued except for a short period from August 1978 to December 1979. The representatives of the Indian Sugar Mills Association and the National Federations of Cooperative Sugar Factories were unanimous that the system of control was necessary in the case of sugar and the mechanism of futures trading would not help the industry or trade. The Sugar Merchants Association, however, pleaded before the Committee that if there was to be complete decontrol of sugar, the facility of futures trading may be provided.

74. Taking into account the special circumstances in which the market in sugar functions, the Committee recommends that there is no need for futures trading in it. If, however, the present pattern of marketing of sugar is to give place to a system of free market, then the case for futures trading could emerge as a machanism which would provide the advantages of such trading to the various functionaries in the trade. It would also then be of benefit to the producers and consumers.

75. As regards gur, the representatives of the trade were unanimous that futures trading should be allowed in this commodity. They were of the view that such trading in the commodity in 1979 had benefitted all the interests including the producers and in the absence of such a facility the prices of gur would have declined unduly. It was further stated that stock holding of gur helped both the crushers and consumers as the bulk of the arrivals of the commodity took place within three to four months while consumption was spread over the entire year. The holding of stocks required the facility of hedging to cover against adverse price fluctuations. It was argued that if there was hedging facility, there would be more stock holders, more competition and reasonable levels of prices. In the absence of futures trading, stock holding will be resorted to only by a few financially powerful operators who could speculate with their stocks and influence prices.

76. The Committee has considered the claims advanced in respect of futures trading in gur. It is to be noted that there are some crucial factors which make gur prices behave differently from sugar prices. The sugarcane production in the country is subjected to a regular and acute cycle of alternate high and low production periods due to wide variations in its acreage in response to relative profitabilities of competing crops like cotton, wheat and paddy. As demands for sugar and gur are also inelastic to some extent, variations in cane availability lead to sharp fluctuations in their prices. However, while a major portion of sugar coming under the levy scheme has remained controlled at various points from time to time, gur has neither been subjected to any fixed price nor to any other form of control at any point of time. Hence, in periods of shortages when the demand for sugar exceeds its supply, the price of levy sugar does not change but the excess demand is transferred to the gur market, which is free. The gur prices in such a situaiton, register a sharp rise even though sugar prices,

being under control, do not move upwards by any significant margin. Conversely, in times of surplus, the controlled sugar prices do not register much of a downward move, but the full impact is transferred to the gur market and hence gur prices often fall unduly. Such wide fluctuations in gur prices due to recurring cycle in sugarcane production and absence of any effective control mechanism to deal with the situation, seem to make a strong case for futures trading in gur. The fact that the Government had often to resume such trading in the past, particularly during the down-swing of prices, is indicative of the compulsion of permitting such facility in gur. However, the Government had also to suspend such trading, as a precautionary measure, during the acute phase of the up-swing of the price cycle to ensure that futures trading did not in any way accelerate the rising tendency in gur prices. The Government's concern about high prices of gur during the year of short cane crop, arises mainly because the high gur prices often have detrimental effect on the production of sugar. During the period of shortage, high prices of gur have the effect of drawing away cane supplies from the production of sugar to the manufacture of gur as the gur manufacturers are in position to offer higher prices but not the sugar manufactures in view of the fixed price of levy sugar.

77. Other factors in respect of gur which required special consideration are that despite the tradition of futures trading, there are no well-defined and acceptable standards in respect of gur and hence, the grades as understood in different markets, do not have close relationship with one another. This makes it difficult to identify comparable grades and to determine proper prices for them. Secondly, gur cannot be stored for long without deterioration in its quality. These factors often lead to malpractices in regard to fixation of spot and futures rates, due date rates, etc., if the associations under which such contracts are traded are not responsible enough to deal with such problems impartially.

78. In view of what is stated above, we consider that while there is an inherent need for futures trading facilities in gur owing to its large but varying production causing wide price fluctuations, such trading would require much closer supervision both by the recognised association and the Forward Markets Commission. We recommend that futures trading in gur should be permitted as a policy on a continuous basis save in exceptional circumstances brought about by acute shortage of sugarcane, when the Government or the Forward Markets Commission might, if the situation so warrants, suspend it for the time being. Such suspension, however, should be temporary and futures trading should be restored as soon as possible. At the same time when futures trading is permitted in the commodity, it should not be for any specified period (say for one year as was one in December 1978) since that leads to uncertainty and speculation having unhealthy effect on the working of the futures markets. Further, the associations recognised for gur should be such as to be able to deal with the special problems of the commodity, particularly those relating to standardisation and grading, and should have qualified personnel and resources to deal with such problems.

XI. Silver

79. Futures trading as well as other types of forward trading in silver have been banned since January 1963 throughout the country. Prior to that futures trading was regulated in Bombay under the Bombay Bullion Association Ltd., since October 1960, but all such trading was free in the rest of the country.

80. An important factor to be noted is that the country does not produce silver in any appreciable quantity. The annual production is negligible at 20 tonnes approximately. However, the stocks of silver in the country are estimated at about 70 thousand tonnes. Exports of silver were banned in October 1966. The ban was removed in February 1974 but exports were canalised through the STC from August 1976. Ban on exports, reimposed in February 1979, is being continued.

81. The Bombay Bullion Association requested for resumption of futures trading in silver mainly on the grounds that there are large stocks of silver in the country, the concerned interests need protection from price fluctuations, there is a long tradition of such trading in the commodity and silver is not an item of mass consumption.

82. The Committee has considered the case for futures trading put forth by the Bombay Bullion Association. We find that India's production of silver is negligible and its supply is limited. Silver has become a very important industrial raw material and has also acquired strategic importance. As a result, its stocks are getting depleted over the years. Exports of silver are not permitted. Silver market has also become volatile of late with very abnormal variations in prices and these abnormal conditions are expected to continue in the foreseeable future. Taking all these factors into consideration, the Committee is of the view that there is no case for permitting futures trading in silver at present.

XII. Other commodities

83. During our discussions with the trade as well as other Bodies and Departments concerned with various commodities, it was represented to us that the practice of futures trading in India was, so far, confined to certain commodities in which there was a long tradition of such trading. Most of the concerned interests continue to demand facilities for futures trading only in those commodities. However, due to technological developments, availability of more inputs, etc., there has been a substantial increase in the production of many other commodities in excess of internal demand, and often they had to be exported in large quantities. The Government programmes for stabilisation of prices in these commodities were very rudimentary and meagre. As a consequence, the functionaries in the these commodities including producers, suffered heavy losses due to adverse price fluctuations. It was contended that if futures trading in these commodities could be organised, it would serve as advance indicator of future trend of prices to producers to plan their production of the commodities and the much needed hedging facilities would be available to other functionaries also. The commodities

indicated in this regard were cardamom, coffee, tobacco, tea, ginger, chillies, onions, potatoes, apples, etc. We could not study all these commodities in detail for lack of time at our disposal. The position in regard to some of these commodities is as follows :—

Cardamom

84. Cardamom has acquired importance as a foreign exchange earner in recent years. During the decade 1968-69 to 1978-79, the domestic production of cardamom increased from about 2100 tonnes to 4000 tonnes and exports from 1300 tonnes to 2900 tonnes. Thus, the exports now amount to about 70 per cent of the domestic production as against 60 per cent in 1968-69. The foreign exchange earnings from the commodity increased from Rs. 8.93 crores in 1969-70 to Rs. 19.38 crores in 1975-76 and Rs. 60 crores in 1978-79. The production target for 1980-81 is placed at about 5000 tonnes. It was contended by some that production and exports could be increased substantially if the exporters had adequate facilities for advance commitments with the foreign buyers and covering such commitments in the domestic market.

85. The Government of India has established a Cardamom Board under section 4(3) of the Cardamom Act, 1965, principally to ensure remunerative returns to the growers, regulating the sale and exports of the commodity, stabilisation of its prices and improving its marketing. The owners of cardamom estates have to get themselves registered under the Cardamom Act and the various functionaries in the trade are required to obtain licences from the Board. After harvesting, cardamom is sold by auction under the supervision of the Cardamom Board. Although the production of cardamom is not very large in absolute terms, in value terms the commodity assumes importance. From the export angle the commodity is significant since the bulk of the production is exported and the foreign exchange earnings from it are quite sizeable. The commodity has, therefore, a good case for being traded on a futures market so as to provide the much needed hedging facility to the various functionaries particulatly the exporters and stockists. However, some difficulties associated with the marketing of this commodity at present are that there are no adequate cold storage facilities under which condition along the quality of it can be fully preserved. As a result, stocks are not carried forward on any large scale beyond a period of three months or so. The exporters presently purchase cardamom in auction markets, only against their firm commitments. We are of the opinion that these difficulties are not insurmountable and with the building up of the necessary infrastructure, this commodity would become suitable for futures trading. Keeping in view its potential for being traded on the futures market, we recommend that the Commission should keep this commodity under watch and advise the Government regarding introduction of futures trading in it at appropriate time. Once this happens further developments in the marketing structure may get accelerated.

Coffee

86. There has been no doubt a phenomenal increase in the production, exports and internal consumption of coffee. The production has increased from about 73.4 thousand tonnes in 1968-69 to about 123 thousand tonnes in 1977-78. During the said period exports increased from 34.8 thousand tonnes to 60.2 thousand tonnes, Internal consumption rose from about 30 thousand tonnes in 1969 to about 44 thousand tonnes in 1977. However, the marketing of coffee has been under the charge of the Coffee Board consituted under the Coffee Act (VII of 1942). The Board operates the pool system of coffee marketing which covers all coffee estates and the entire crop. The Board at present releases about 40 per cent of coffee production through registered wholesalers, retailers and cooperative societies for internal consumption and about 60 per cent of the production through nearly 60 registered exporters for export purposes. The releases for internal marketing are spread over the entire year through pool sales which are held once a month at three principal marketing centres, namely, Bangalore, Coimbatore and Vijayawada. In regard to exports, coffee allocated for export is sold periodically in open market auctions held once in two weeks in Bangalore. The exporters are expected to export the quantity released to them within the prescribed time limit, which may be extended.

87. Coffee is no doubt suitable for futures trading as it has standardised grades. Futures markets in coffee are functioning for a long time in New York and London. However, the functioning of a broad futures market within the present institutional arrangements for marketing obtaining in our country is not possible since the releases of coffee are controlled and no body else excepting the registered traders are permitted to purchase coffee. In the circumstances, it would not be possible for every operator in a futures market to purchase coffee and deliver against his contract if such a need arises. The question of introducing futures tarding in coffee can be considered only when free trading in coffee is introduced.

Tobacco

88. Tobacco is one of the important commercial crops in the country. It contributes about Rs. 600 crores per annum to the Central Exchequer by way of excise duty and earns foreign exchange of more than Rs. 100 crores per annum on the quantity exported. The main varieties grown in the country are Virginia Flu Cured (VFC) and Bidi Tobacco. While VFC is used in the manufacture of cigarettes and also export oriented (about 90% of the total exports are of the VFC variety), Bidi Tobacco is primarily used for domestic consumption. The production of tobacco in the country, however, is subject to periodical gluts and shortages as will be seen from the following table :—

Year	Production (Million kg)
1973-74	462.1
1974-75	363.1
1975-76	349.8
1976-77	418.8
1977-78	493.6
1978-79	451.2

Source : Directorate of Economics & Statistics, Ministry of Agriculture & Irrigation, Government of India.

The production of both VFC and Bidi Tobacco during 1977-78 season exceeded the overall demand and created marketing problems. The price support operations initiated by the Government through the STC and NAFED could not be on a very extensive scale to be beneficial to producers.

89. At present the marketing pattern in vogue in respect of tobacco is in a very rudimentary stage. Though the Tobacco Board, established in 1976 has initiated some steps to introduce proper grading of the various varieties of tobacco grown in the country, grading is not done at the primary level and there are no organised competitive ready or auction markets where producers can sell their produce at competitive prices. While it is always open for the producers to take back their produce brought by them to the platforms of individual manufacturers or exporters if they do not agree to the gradation made or prices offered by the buyers, generally they are not in a position to do so. The number of cigarette manufacturers using VFC tobacco are only 4 in the country and the international market also, the number of importing companies which really matter are limited in number. These buyers are very selective and are in a position to dictate their terms. Even the non-manufacturer exporters are often unable to get adequate price for the tobacco which they have purchased from the producers and which they are not in a position to export. There is no large class of professional commission agents buying or selling the commodity on their own account or prepared to assume the speculative risks involved in the marketing of the commodity. As a consequence of all these factors, the price paid to tobacco producers is reported to be generally quite low and often unremunerative.

90. The Tobacco Board, to ensure that the produce is not exported at throwaway prices, fixes the minimum prices for exportable tobacco. However, there is no system of support prices for purchases from producers. At present even trading in actual tobacco on forward basis (i.e. trading through ntsd contracts) has not developed in the internal market on any large scale. Exporters often purchase their tobacco in the internal market against firm commitments made to the foreign buyers. The important points to be noted in respect of this commodity are that the supply of tobacco is large and there have been wide fluctuations therein. Further, the demand is uncertain since a part of it comes from overseas buyers. Fluctuations in the prices of the commodity are quite large and the growers generally do not get remunerative prices. Though the present system of gradation is not fully satisfactory, the commodity is amendable to a proper system of grading. On the other hand the present market structure is imperfect in the sense that the manufacturer buyers are limited in number and they are in a position to dictate terms to the sellers. In fact, many of the imperfections in the marketing system of tobacco seem to have grown in the absence of proper organised markets both for ready and forward transactions. In the above context, the Committee is of the view that the commodity being suitable for futures trading, it would be advisable for the Tobacco Board and the concerned interests to take early steps to provide a proper system of ready and futures markets in the commodity.

Tea

91. The question of the need to introduce a futures market for tea in India was recently considered by the Committee on Tea Marketing which has already submitted its Report to the Government. The Committee has pointed out that though tea is the only important agricultural produce which does not have a futures market possibly because of the diversity of its qualities, there is a growing school of thought in the U. K. favouring a futures market for tea to provide an acceptable price indicator and help reduce price fluctuations.

92. The production of tea in the country is large and a substantial quantum is exported annually. There are also gluts and shortages in this commodity leading to large variations in its prices. The commodity being export oriented the facility of futures trading would be to the advantage of the exporters and will contribute to export promotion. The Committee has noted the fact that there are innumerable qualities of tea. However, it should be possible to evolve a suitable futures contract for a representative quality and to operate it in such a manner as to make the hedging facility available in respect of the other representative qualities, as well. The necessary institutional framework would have to emerge before the actual opening of futures trading. The Committee, therefore, recommends that the Tea Board and the concerned interests should work towards the evolution of such a framework so that futures rading in tea is possible.

93. The Committee has considered the suitability of various other commodities like potatoes, onions, apples, ginger, chillies, etc. for futures trading. The supply position of these commodities has been comfortable in recent years with significant increases in their production. In fact, in commodities like potatoes, onions, and even apples there have been gluts leading to uneconomic prices to the growers. This has led to short-fall in production and consequent very high levels of prices in the subsequent year adversely affecting the interests of the consumers. Such a situation has developed apparently because of the absence of proper marketing mechanisms. The functionaries which can absorb the shocks of surplus and lean seasons are not in existence since they have no method by which to cover their own risk. There is no doubt that the existence of futures markets will provide for the coverage of such risks adequately and enable the stockists and dealers to act as a cushion in periods of excess production and shortages. Some of these commodities need adequate storage facilities for the holding of stocks over a long period. The introduction of futures trading may itself help to some extent the process of building up the necessary infrastructure required for efficient marketing. The Committee, therefore, recommends that these commodities too should be kept under watch by the Commission so as to take timely steps for introducing futures trading in them.

CHAPTER 5

BASIC REQUISITES FOR THE REGULATION OF FUTURES TRADING

Suitable representative association sine quo non of futures trading

The fulfilment of economic and technical requirements in respect of any given commodity alone is not enough for the satisfactory conduct of futures trading in it. A body or association representing functionaries having genuine hedging interests such as growers, dealers, stockists, processors, exporters, importers and consumers on the one hand and commission agents, brokers and experienced speculators prepared to assume the risk involved in the marketing of the commodity on the other, must come forward for organising such trading. The principal requirements to be fulfilled by an association are :—

(i) it should be a representative body not dominated by any sectional interest;

(ii) its membership and the clientele of members must together be large enough to make the futures market broad and competitive;

(iii) it must provide a trading ring with essential amenities in which its members and others can carry on their trading operations in a competitive manner;

(iv) it must make rules and regulations with a view to establishing fair trading procedures, proper standards or grades, a system of inspection, arbitration and survey machineries, etc.;

(v) the association must have an efficient secretariat manned by competent staff capable of impartially executing the rules and regulations without fear or favour;

(vi) it should be in a position to collect and disseminate relevant information regarding the concerned commodity.

2. We are of the view that the maintenance of competitive character of a futures market should be the most important consideration in the regulation of futures trading. The principal benefits attributed to futures trading are based on the assumption that futures markets make the closest approach to conditions of pure competition visualised in economic theory as they involve a very large number of traders dealing in the commodity with standard contracts, the provisions of which are widely known and understood. The main objective of a regulatory policy should, therefore, be to promote as much fair competition as possible in the working of the futures markets. The various aspects regarding regulation of futures trading such as the location of centres for establishing futures markets, selection of suitable associations for conducting trading at the centres, rules and regulations subject to which such trading should be permitted, regulatory measures that may be introduced by the Commission to contain excessive speculation, etc., need to be considered from this point of view.[1]

Choice of centre for location of recognised association

3. The choice of a centre for the location of a futures market has a very important bearing on the competitive character of the market. Futures trading in a commodity has a tendency to get concentrated at terminal centres as hedgers generally prefer to trade at those centres where cost of hedging is relatively lower on account of the large volume of trading. The cost of hedging consists of (i) brokerage charges for executing the transactions at the time of entering into and squaring up the contracts, and (ii) the 'bivalence'[2] i.e. the difference between the buying and selling quotations that exists at any given point of time, in all future markets. Both the brokerage charges and the bivalence are the minimum in that futures market which is most competitive compared to other markets. The terminal markets are generally more competitive than the interior markets as the associations conducting futures trading at such centres have generally a large membership of more than a couple of hundred members besides many floor brokers operating in their rings. Upcountry clients also prefer to trade at such centres in view of the availability of various facilities and a large number of brokers to put through their transactions. The Commodity Exchange Act in the U.S.A. requires that the futures markets to be designated under the Act shall generally be located at the terminal centres only as will be seen from the following provision in the Act : "Sec. 5" The Commission is hereby authorised and directed to designate any board of trade as a "contract market" when, and

[1]The Commodity Futures Trading Commission of the U.S.A. has brought out this aspect clearly in its Annual Report of 1978. It says, "the Commission plays a vital role in the fostering of competitive markets and trade practices in order to protect the utility of future markets within the economy and to simultaneously protect market users and consumers. Before any contract market can be established the Commission must review the proposed terms and conditions of the contract to ensure they are both consistent with commercial practices and not contrary to the public interest".

[2]In ready transactions generally a merchant tends to buy at 'bid' prices and sell at the 'higher' prices which he asks. In the futures market, on the other hand, he tends to buy at the price 'asked' for and to sell at the 'lower' bid price. The merchant is paid for his services to processors and exporters by receiving an 'asked' price and he in turn is willing to pay for corresponding services of brokers in the ring (ring traders or tarauniwallas) in the futures market by buying often at 'asked' price. For details, see Holbrook Working—'Futures Trading and Hedging', American Economic Review, June 1953, Pages 332—337.

only when, such board of trade complies with and carries out the following conditions and requirements :

(a) When located at a terminal market where any cash commodity of the kind specified in the contracts of sale of commodities for future delivery to be executed on such board is sold in sufficient volumes and under such conditions as fairly to reflect the general value of the commodity and the differences in value between the various grades of such commodity, and where there is available to such board of trade official inspection service approved by the Secretary of Agriculture or the Commission for the purpose : Provided, that any board of trade not so located shall be designated as a "contract market" if such board of trade provides for the delivery of commodities on such contracts at a delivery point or points and upon terms and conditions approved by the Commission. (As amended by Act of October 23, 1974 (Commodity Futures Trading Commission Act of 1974), effective April 21, 1975, Sec. 103, 88 Stat. 1392.)"

4. In India, however, we have been permitting the establishment of futures markets at a number of centres in the same commodity. This has resulted in recognised markets becoming very thin making it easy to resort to malpractices such as temporary squeezes and corners and short-term manipulation of futures prices. It may be noted that futures trading in the United States permitted in about 55 commodities (Annexure XI) is conducted under the auspices of only 11 designated markets. On the other hand, in India a great deal of fragmentation of markets often occurs as futures trading in a single commodity is permitted at a large number of associations located at different centres. For instance, at one time there were as many as 18 recognised markets for cottonseed, 14 for gur, 9 for groundnut and 12 for groundnut oil.

5. The Dantwala Committee in its Report has made the following observations in this regard :

"The argument in favour of a large number of centres to cater to the local requirements of variety etc. rests on a misconception of the nature of the futures market. It is precisely to obtain an escape from the (local) constraints of specific varieties, etc. that the futures market is organised through a system of trading in a 'basis' variety ....." "Futures trading of our conception and which, we hold, has a positive economic contribution to make to orderly marketing, is **not a small town business.** If, in spite of this, there is a clamour for the establishment of futures markets in every town in an area, the effort should be to wean away the people from what is no more than a dubious opportunity to earn a living, rather than yield to the clamour ....." " In our view, generally **there need not be more than one futures market for commodity in a region** ....." "It would follow from what is said above for the region that there should be only one recognised association for futures trading in one commodity in a single city or town."

(Paragraphs 6.11 to 6.16 of the Report of the Forward Markets Review Committee—October 1966).

6. We are in complete agreement with these views. The choice of a centre for the location of a futures market should be mainly governed by the liquidity and the competitive character of the market along with such other considerations as the importance of the centre from the point of view of the ready trade in a commodity, availability of financial facilities in the form of banks and other financial institutions, importance of the place as export/import centre, etc. However, a centre which satisfies all other requirements such as importance in spot or ready business, availability of banking and transport facilities, etc. but is not likely to develop into a very broad competitive market due to lack of large membership, reluctance on the part of a large number of non-member clients to do business at the centre either due to lack of confidence or adequate communication facilities, etc., cannot become a competitive market. We, therefore, recommend that, as far as possible, the number of recognised futures markets in any commodity should be limited to the minimum necessary to avoid dispersal of hedge and speculative business over a number of markets making them in the process thin and less competitive. This would also facilitate more effective regulation of the recognised markets by the authorities concerned.

7. After a centre is recognised for futures trading, every effort should be made to preserve and encourage its competitive character. From this point of view, we consider that the present provision in section 15(4) of the FC(R) Act of permitting members to appropriate the business of non-member clients, although with their consent, is not conducive to maintaining the competitive character of futures trading. Under the present provision, a member is permitted to appropriate i.e. to enter into an opposite contract on his own account with the non-member client with the client's written consent. The requirement of obtaining a written consent is observed by obtaining a 'general consent' from his customer as it is extremely difficult to obtain a written consent every time. In case, the member does not desire to appropriate the business himself, he matches the opposite order of another customer of his choice with the order of the first customer. This means that a large part of futures business gets transacted outside the ring of the association recognised for the commodity. On the other hand, in most of the futures markets all over the world, particularly in the U.S.A., the principle that all futures contracts should be entered into openly by an out-cry in the trading ring, is adhered to very scrupulously. If the business of non-member customers is appropriated by members or matched with other customers outside the ring, then the impact of such business is not felt on the trading in the ring and the futures prices determined in the ring to that extent are less competitive. Since a large volume of business in futures contracts is between members and non-members, the competitive character of the futures prices suffers severely to that extent in

India. We, therefore, recommend that the present provision of permitting members to appropriate non-members' business outside the trading ring should be deleted and the FC(R) Act as well as rules and regulations of the recognised associations should provide that all business of non-members shall be put through in the ring by an out-cry and any member of the association should have an opportunity to enter into an opposite transaction with the non-member at the most competitive rate offered in the ring.

Instruments of regulation

8. The question of the choice of regulatory measures to be adopted by the Commission to avoid any manipulative activity in the futures markets through excessive short or long speculation is also to be looked at from the point of view of maintaining the utility of the futures markets for the purpose of hedging for which they have been established and their competitive character. As has been explained in Chapter 2 (paragraph 12) hedging with a view to insuring against adverse price fluctuations in the actual commodity market is practicable when ready and futures prices move in a parallel way and rise or fall, more or less, to the same extent. It, therefore, follows that the regulatory measures designed to keep futures prices only in check are likely to impair the utility of the futures markets for the purpose of hedging.

9. The various regulatory measures adopted by the Forward Markets Commission to regulate futures trading are described in Annexure XII. The question of the efficacy of these regulatory measures was discussed in paragraph 5.28 to 5.35 of the Dantwala Committee's Report. It is observed in paragraph 5.33 of the said Report, "In brief, we suggest : (a) that regulatory measures should be applied sparingly, taking a certain amount of calculated risk; (b) that it is better to ban futures trading than to permit it in a crippled form, divorced from the conditions in the spot market and (c) that in applying regulatory measures, a sharp distinction should be made between the need to curb unhealthy and unlawful trading practices and the fulfilment of an economic policy like restraining price rise". We are generally in agreement with the views expressed in that Report. We feel that since the futures market is primarily established to offer hedging facilities to the trade, the Commission's measures should not be such as to impair the utility of these markets for the purpose of hedging. If the regulatory measures distort proper relationship between ready and futures prices, then the very purpose for which the markets are established is defeated. In such circumstances, the market would appear to be continued under the regulatory measures only for the benefit of speculators as hedgers would remain out in view of their inability to off-set their losses in the ready or the futures market by corresponding gains in the futures or the ready market. Similarly, since the efficacy of the functioning of the futures market as a whole also depends upon the competition and the liquidity of the market being protected, any regulatory measure which reduces competition and liquidity or tilts the balance in favour of certain groups as against others should be avoided. We are of the view that while reasonable restrictions on speculative open positions as opposed to hedge open positions and reasonable limits on periodical fluctuations in prices are in conformity with the basic purpose for which futures markets are established, the very stiff special margins linked with the futures price levels and the maximum and minimum prices only in respect of futures contracts should be examined critically and in any case used sparingly.

Statutory return as an instrument of effective regulation

10. The proper functioning of futures markets established under the auspices of recognised associations cannot be taken for granted and **effective supervision** by the Forward Markets Commission is the most important requirement of ensuring that the established markets adhere to their rules and regulations and the standards laid down by the Commission. The FC(R) Act empowers the Government to nominate its representatives on the governing bodies of the recognised associations, to hold enquiries into their working, to require members of the recognised associations to maintain proper accounts and prescribed documents for a period of three years and to inspect these accounts and relevant documents, to require the associations to obtain approval of the Government to amendments to their rules and regulations, to suspend members and to supersede the governing bodies. Many of these powers have been delegated to the Commission and one of the directors nominated on the governing bodies is an officer of the Commission. Periodical discussions with authorities of the recognised associations and keeping a regular watch on the trading in the rings of the associations also help to improve the working of the recognised markets. While this is being usually done by the Commission, we would like to point out that a prompt, regular and adequate system of reporting their operations by different operators in the futures market is the primary condition of any effective supervision. At present, the Commission requires members of recognised associations to submit returns normally on weekly basis and, in special circumstances, on daily basis. The proforma prescribed for this purpose requires a member to show separately his brought forward position, his purchase and sale operations for each day of the week and the names of the non-member clients and their operations. This system of reporting, we consider, defective in many ways. First, it does not bring out the most vital information regarding the extent of hedging for which the markets are established. This information can be obtained by requiring **each operator** to disclose the break-up of his open position as hedge position and speculative position separately as specifically defined in the proforma to be prescribed as is being done under the Commodity Exchange Act of the U.S.A. This should be a **statutory requirement** so that there is no question of anybody challenging the requirement on the ground that vital business information is being obtained by the Forward Markets Commission without any statutory powers. The procedures to be laid down by the Commission in this regard would, no doubt, ensure that the information furnished is kept strictly confidential. Secondly, the present practice of requiring members to indicate the trading details of their non-member clients is not likely to bring

forth correct information. Apart from the fact that non-members may be trading through more than one member and that this would make it somewhat difficult in the Commission's office to aggregate the positions so held and controlled by the non-members trading through different members, it is somewhat unfair to make a member vouch for the correctness of the trading details of a non-member. We, therefore, recommend that a periodical return on the lines indicated in the proforma given in Annexure XIII may be prescribed by the Forwards Markets Commission and all operators—members as well as their non-member clients—should be required to submit it to the Commission. While the Commission may revise the proforma as per requirements, the disclosure of the break-up of the total open position into hedge and speculative positions should, in any case, be its permanent feature.

11. We also recommend that in a commodity in which more than one futures markets have been established initially, even when such markets are few, their continuance should be periodically reviewed on the basis of the extent to which the established markets have been used for the purpose of hedging.

Business of non-member clients

12. One aspect of futures trading which requires special consideration is the question of properly regulating the dealings of non-members. Under the FC(R) Act when futures trading in a commodity is regulated by Government by applying section 15 of the Act to the commodity, only futures contracts entered into between, through or with members of recognised associations are legal. This means that persons who have not become members of a recognised association can enter into such contracts only with or through the members of the recognised association. Barring the requirement in section 15(4) relating to appropriation of the business of non-members by members, there are no other direct provisions in the FC(R) Act either to control the activities of non-members or to give them adequate protection against the manipulative activities of members.

13. Since many of the manipulative tendencies in the futures market arise through trading in the name of non-members, fictitious or benami, it is desirable to have a more direct control on the activities of non-members than at present. This can be achieved by requiring all non-members desirous of trading in a futures market, to register with the Commission through the concerned recognised association subject to such rules and conditions as may be prescribed by the Commission for the purpose. We have already recommended in paragraph 10 of this Chapter that all such non-members trading in the futures market should submit their returns disclosing their trading details to the Commission directly in the prescribed proforma. These returns, along with the returns submitted by members showing their own trading details as well as the trading details of all their non-member clients, will enable the Commission to get a complete picture of the trading operations in the market.

14. We also recommend that the recognised associations should be required to lay down in their rules, certain minimum margin or deposit, ranging between say 5 to 25 per cent of the value of the contract, to be obtained by a member from each non-member. The minimum deposit could be varied by the Commission within the prescribed range, if the situation so warrants, keeping of course in view the requirement of maintaining the competitive character of the market. At present, the payment of minimum margin by each and every non-member client is not compulsory and as a result, a member can accommodate a number of buyers and sellers of insufficient means by himself paying to the association some deposit or margin on his net open position arrived at after offsetting long and short business of a number of clients. The requirement of minimum margin payable by each client separately on his own business would eliminate clients of insufficient means, and would also make the clients paying such margins more vigilant about their rights and the manipulative activities of members against them.

15. Under the present FC(R) Act there is also no protection to non-members in respect of their margin amounts, if any obtained by the member from such non-member. It should be laid down in the Act that the margin amounts collected by members should be held in segregation by the member concerned and not commingled with his own funds. The Act gives powers to the Commission to examine books of accounts and other documents of members. These and such other powers as are given to the Commission under rules and regulations of the association should be utilised by the Commission, as is being done by the Commodity Exchange Authorities in the U.S.A., to ensure that the deposits of non-members are held in segregation and not used for personal purposes by them.

16. We understand that on many occasions, running hedge contracts under the auspices of the recognised associations are suddenly closed out by the members acting in concert or by the Boards of recognised associations before the actual due date of the contract, at rates arbitrarily decided upon. This is highly injurious to the trading as well as the financial interests of other operators, particularly the non-member clients. The Committee, therefore, recommends that the rules and regulations of the recognised associations should make special provisions to prevent these types of malpractices and such activities on the part of any association should be considered serious enough to justify the withdrawal of recognition of such an association.

Need for long term policy

17. Having recommended continuation or immediate resumption of futures trading only in such commodities in which it is economically and socially desirable and also introduction of a proper scheme of regulation, we would recommend that the Government should adopt a long-term policy in respect of futures trading. Once it is permitted, it should be continued without any interruption except in very abnormal situations when it might be necessary to suspend it in a particular commodity for a short period. However, before considering even such temporary suspension, other alternatives such as skipping over some nearer deliveries and permitting trading in more suitable distant deliveries, which could meet the needs of the situation, should be explored. It should be borne in mind that

markets take time and sometimes decades to be built up and, therefore, futures trading in a given commodity should be a long-term consideration.

18. We have already emphasised that beneficial futures trading can be organised only through the medium of a representative association. It is, therefore, essential for the Governmental Regulatory Authority to concentrate its attention on developing and nursing the associations, once they are carefully selected and recognised, into modern commodity Exchanges. A modern commodity exchange in Europe or in America is a highly organised and efficient institution terminally located which gives a central price picture for the commodity traded on its floor. In a country there may be hundreds or even thousands of primary or secondary markets for a commodity, the prices in which are largely governed by local supply and demand situations. The market under a commodity exchange, however, should have a national character if the pricing procedures practiced under its auspices are to result in what we may call the most representative price which could serve as a guide for allocating supplies of the commodity over time and if the exchange is to serve the country as a forum for vital market information in the concerned commodity. For discharging this central role in the price formation process and the dissemination of all relevant information, the exchange has to enjoy a reputation for fair competition, integrity and sound ethics. The famous Commodity Exchanges of Europe or America have evolved as central marketing places over a hundred years at principal cities like New York, Chicago, London, Liverpool, Winnipeg, Antwerpe[1], etc. They are housed in multistoried buildings of their own with excellent trading halls having modern communication and other facilities, have well equipped secretariates with qualified administrative staff, recognised expert appraisers or surveyors to determine quality or grades in relation to standards fixed by them or the Government and adequate inspectorial staff to licence trade godowns and inspect grades and qualities of the concerned commodities[2]. Thus, these exchanges have become nerve centres of the country's commerce by evolving operational patterns and functions which are being revised and refined to a high degree of perfection needed for modern commerce. We suggest that it should be the endeavour of the Government and the Forward Markets Commission to develop the associations recognised for futures trading in the country into such modern commodity exchanges. We hope that the existing associations will take heed of these suggestions and strive towards such institution building.

[1]The Chicago Board of Trade, the largest Exchange in the world, was established in 1848, the New York Cotton Exchange in 1870 and the Winnipeg Grain Exchange in 1908.

[2]Two-third of the area of the specially designed trading floor of the Chicago Board is devoted to futures trading. The remaining one third of the floor comprises the cash market. The floor of the futures trading has different pits or rings for trading in different commodities. Special arrangements are made to ensure that all hear the bids and offers that are cried out. The market reporters are posted at strategic points to observe change in prices and send these to a centre point wherefrom it is put on the ticker system for transmission throughout the world in a few seconds. The secretariat, besides administrative staff, consists of several departments such as (1) Department of Investigation and Audit, (2) A Transportation Department, (3) Inspection Department, (4) Statistical Department etc.

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CHAPTER 6

NON-TRANSFERABLE SPECIFIC DELIVERY CONTRACTS

Nature of ntsd contracts

A non-transferable specific delivery (ntsd) contract has been defined under the Forward Contracts (Regulation) Act, 1952 (FC(R) Act) as a specific delivery contract, the rights or liabilities under which or under any delivery order, railway receipt, bill of lading, warehouse receipt or any other document of title relating thereto are not transferable. As explained in paragraph 7 of Chapter 3, this contract is meant for actual marketing of the commodity over time. The giving and taking of delivery is not optional but compulsory. The contract, however, is classified under the Act as a forward contract since it contemplates delivery after eleven days which is the period prescribed for completion of delivery in respect of a ready contract. A typical ntsd contract lays down in its specific terms the quantity and quality of goods to be delivered, the price of the goods, the period of delivery and the names of the buyer and the seller. Thus an ntsd contract is akin to a ready delivery contract except that the delivery of the goods and payment therefor are made after 11 days.

2. As mentioned in paragraph 12 of Chapter 3 whether the ntsd contracts should be regulated as a rule or whether they should be kept outside the purview of the Act was a point which attracted considerable attention of the Expert Committee (Shroff Committee) and of Parliament at the time of placing the present Act on the statute book. The Bombay Forward Contracts Control Act, 1947 required that not only transferable contracts including futures contracts but also ntsd contracts in the commodities to which the Act had been applied, should be regulated through the associations recognised for the purpose under the Act. The Expert Committee on Futures Markets (Regulation) Bill, 1950, however, felt that since ntsd contracts were of a different category and since such contracts could not normally be used for speculative purposes, it would cause serious inconvenience to the trade and make normal trading practically impossible if such contracts were not exempted from the restrictions applicable to the other two types of forward contracts. The Expert Committee, therefore, recommended that such contracts should be left outside the purview of the regulation but the Government should have powers to impose such regulations as it might deem fit on such contracts where there was positive evidence about their misuse. The Select Committee to which the Forward Contracts (Regulation) Bill, 1952 was referred also felt that the regulatory provisions of the Bill should not be made applicable to ntsd contracts at all except to the extent to which such contracts were likely to be misused for speculative purposes.

3. The present position, therefore, is that the FC(R) Act exempts ntsd contracts from the regulatory provisions of the Act though formation of an association providing facilities for the performance of such contracts without having to give or receive actual delivery of goods is prohibited. The Central Government is, however, empowered to apply the regulatory or prohibitory provisions of the Act to ntsd contracts in any commodity and in any area where it thinks that such a step is necessary in the interest of the trade and in the public interest.

Need for ntsd contracts

4. The need for the facility of ntsd contracts to various trade interests (dealers, commission agents, processors, manufacturers, etc.) arises mainly for ensuring in advance a smooth and assured supply of and demand for the commodity in the future period.

5. Though dealers, crushers, manufacturers, etc. generally carry some stocks to provide for their immediate requirements, it is not economical to carry actual stocks of large quantities on account of storage problems and cost of carrying such stocks. The ntsd contracts enable the buyers to make arrangements for continuous supply of the specific types of goods without being required to carry large stocks over time; similarly, these contracts enable the sellers to sell in advance the specific types of goods they may be possessing or are likely to possess or manufacture in future. Though a certain quantum of commitments in ntsd contracts are made as a routine, the expectations of the concerned trade interests regarding the future course of prices play a major role in determining their total quantum of buying or selling through these contracts. The interests which expect the prices to rise would buy and those which expect the prices to fall would sell at the current prices for taking or giving delivery at a future date.

6. A large proportion of buying and selling in the commodity markets is through the medium of ntsd contracts of duration of two to five months though contracts of much longer duration, particularly in manufactured commodities like cloth, steel or tools, are also often entered into. It is to be noted that such trading in a commodity often exists independently of whether or not futures trading exists in the commodity[1].

7. The procedure for entering into such contracts, however, differs from commodity to commodity and from region to region. Broadly speaking, there are two types of systems, 'katcha adat' system and 'pakka adat' system. In the case of 'katcha adat' system, an ntsd contract is entered into by a terminal buyer (manufacturer, processor, end-user, etc.) with an upcountry stockist or dealer through a broker, who acts simply as an agent and is not in any way responsible either to the buyer or the upcountry seller for the

[1]Purchases and sales through ntsd contracts are often hedged in a futures market if such a market exists in the commodity.

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performance of the contract. In the case of 'pakka adat' system, ntsd contract is entered into between a terminal buyer and the upcountry seller through a commission agent, who acts as a principal to both the seller and the buyer[1]. There is no privity of contract between the terminal buyer and upcountry seller and the commission agent is responsible to both the parties for the performance of the contract. Ntsd contracts, except those entered into locally, are made in respect of cotton, oilseeds, oils, raw jute, jute goods, etc. mainly on the basis of 'pakka adat' system.

Steps taken to prevent misuse of ntsd contracts

8. The experience of the Forward Markets Commission (Commission) in regard to the manner in which ntsd contracts were used for camouflaging futures trading in banned or regulated commodities has been described in paragraph 13 of Chapter 3 of this Report. Due to various loopholes in the definition of ntsd contract in the FC(R) Act, stated in paragraph 28 of Chapter 7 of this Report, it became extremely difficult for the Commission to successfully prosecute the parties conducting futures trading in banned or regulated commodities in the guise of ntsd contracts. The problem of illegal forward trading conducted in the name of ntsd contracts became so acute that the Government, on recommendations of the Commission, had to take the following steps from time to time.

(i) In a large number of commodities ntsd contracts were either prohibited by applying section 17 of the FC(R) Act or were not permitted to be traded in the commodities to which section 15 of the Act had been applied.

(ii) In certain commodities, in which the facilities were needed mainly by producers and to some extent by processors, etc., ntsd contracts such as those entered into by farmers for sale of their produce, by manufacturers like ginners, crushers for purchase of their raw material, etc. were exempted from the prohibition. (A list of commodities in which ntsd contracts are banned or not permitted is at Annexure XIV).

(iii) In a few important commodities such as cotton, groundnut and groundnut oil, trading in ntsd contracts was regulated under the auspices of the associations recognised under the FC(R) Act as a result of which such contracts could be entered into only between, through or with the members of the recognised associations. Subsequently, with the emergence of acute shortage and consequent imposition of formal or informal restrictions by certain States on the movement of groundnut and groundnut oil, ntsd contracts in them were suspended. The regulation of ntsd contracts in cotton by the Commission is, however, continuing.

9. We have considered this problem in all its aspects and come to the conclusion that permanent ban or prolonged suspension of ntsd contracts is no solution to the problem. While suspension of ntsd contracts for a short time when there are zonal restrictions on the movement of the commodity can be justified as in that case ready delivery contracts of 11 days duration may be adequate for trading within a zone, an outright ban or prolonged suspension cannot be justified in view of the major role of these contracts in the actual marketing of a commodity for the reasons mentioned in paragraphs 4 to 6 of this Chapter. The absence of facilities for ntsd contracts may create artificial shortages particularly in consuming regions and gluts in producing regions and thus render efficient and orderly marketing difficult, or next to impossible. It was reported to us that even the genuine functionaries handling actual commodities were, these days, circumventing prohibition on ntsd contracts by taking recourse to such dubious devices as recording the dates of entering into the contracts only after receipt of the goods contracted for. In many cases, though the contracts were entered into well in advance of the dates of delivery, the dates of contracts were recorded subsequently so as to show that the contracts were performed by delivery within 11 days, which is the period prescribed for the performance of ready delivery contracts. We were told that such practices were adopted widely in the foodgrains and oilseeds trade. It is clear to us that the prolonged prohibition of ntsd contracts is causing genuine hardships to important functionaries in different commodities and has driven them to practise procedures which they would otherwise not like to adopt. The fact that these contracts were used by some for camouflaging their speculative trading cannot really be an argument to deny the facility to the sections of the trade which need it for genuine purposes. We have already recommended in Chapter 7 that the present scheme of the FC(R) Act enabling the Government to regulate ntsd contracts, when necessary, should be retained. We consider that, along with other amendments suggested by us, this is an adequate safeguard to control any possible use of ntsd contracts for speculative purposes.

10. During the course of regulation of ntsd contracts in cotton, groundnut and groundnut oil, the Commission has evolved a comprehensive scheme of bye-laws which not only prevents settlement of these contracts without taking or giving delivery except for 'force majeure' reasons but also aims at controlling the use of these contracts for acquiring hold over a large quantum of future supplies. The various powers under the bye-laws enable the recognised associations as well as the Commission *inter alia* to limit the duration of these contracts, impose quantitive restrictions on sales or purchases and restrict the number of intermediaries through classification of members into functional panels. The members of recognised associations can also be required to submit statements of their transactions for scrutiny of the Commission whenever necessary. The Commission's experience of regulating these contracts has been very satisfactory.

11. Taking all these factors into account, we recommend that the prohibition imposed on ntsd contracts

[1]Certain problems arising from adoption of this system on account of the existing definition of ntsd contract have been dealt with in paragraphs 30 and 31 of Chapter 7 and appropriate amendments to the definition have been recommended therein.

in important commodities (like major edible oilseeds such as groundnut, mustardseed and cottonseed and their oils, coconut oil and foodgrains, which are no more subjected to zonal restrictions) should be lifted and such contracts in these commodities should be permitted under the auspices of properly selected recognised associations representing different functionaries dealing with the actual commodity.

12. The principles followed by the Commission in selecting associations for recognition in respect of ntsd contracts such as importance of the centre as a market for ready and ntsd contracts, composition of the membership of the associations, past performance of the associations in regulation of ntsd contracts, readiness of their governing bodies to undertake the responsibility of providing adequate facilities for genuine ntsd contracts, etc., have been stated in the Commission's Report on the Recognition of Associations in respect of NTSD contracts in Indian Cotton submitted to the Government in April 1972. We are generally in agreement with these principles and would, therefore, recommend that the Commission should proceed on the basis of these principles for regulating ntsd contracts in important commodities in which such contracts cannot be permitted freely. The need for continuing regulation of these contracts in the commodities in which they have been regulated should be examined by the Forward Markets Commission at regular intervals and necessary recommendations made to the Government.

13. In the case of commodities other than major commodities mentioned above, we recommend that trading in ntsd contracts may be permitted freely after the amendments proposed in this Report to the definition of ntsd contract and other related matters have been carried out. The Forward Markets Commission should keep a watch on the working of such contracts through its Enforcement Directorate. If the facility for free trading in ntsd contracts in any of these commodities is found to be misused by unscrupulous elements for speculative purposes, the question of bringing them under regulation should be considered by the Commission as and when necessary.

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CHAPTER 7

AMENDMENTS TO THE FORWARD CONTRACTS (REGULATION) ACT, 1952

One of our terms of reference is to suggest amendments to the Forward Contracts (Regulation) Act, 1952 (FC(R) Act) particularly with a view to efficient enforcement of the Act to check illegal forward trading. It is, therefore, necessary to review the experience gained by the Forward Markets Commission (Commission) in administering the Act and the adequacy of the present provisions in the Act for dealing with the problem of illegal forward trading in the light of the experience.

2. The classification of different types of contracts and the scheme of their regulation under the FC(R) Act has been explained in detail in paragraphs 6 to 15 of Chapter 3. Broadly speaking, for the purpose of the Act, the commodities can be divided into three categories. In the first place, there are commodities in which forward trading is totally prohibited under section 17 of the Act. Secondly, there are commodities in which forward trading is regulated under section 15 of the Act. In these commodities forward trading can take place only under the auspices of the associations recognised for the purpose and these commodities are the main target of regulation by the Commission. Finally, there are residual commodities in which forward trading is neither prohibited nor regulated and the only restriction on forward trading in such commodities is that if such trading is controlled or regulated by any association, such an association must have obtained a certificate of registration from the Commission under section 14B of the Act. The category of registered associations was created by an amendment to the Act made in 1960 with a view to enabling the Commission to have a census of all associations conducting forward trading and to ensuring that they did not misuse the facility for free trading given to them under the Act. Under section 18(1) of the Act, non-transferable specific delivery (ntsd) contracts are exempted from the regulatory provisions of the Act, though the formation of an association for providing facilities for the performance of such contracts without giving actual delivery of goods, is prohibited. However, under section 18(3) of the Act, the Central Government is empowered to apply the regulatory provisions of the Act to ntsd contracts in any commodity and in any area whenever it thinks that such a step is necessary in the interest of the trade and in the public interest.

Amendments made to the FC(R) Act in the past

3. After it was enacted in 1952, the FC(R) Act has been amended thrice viz., in 1957, in 1960 and in 1971.

(i) Amendment in 1957

4. The amendment made to the Act in 1957 was limited to the insertation of a new section viz., section 9A. The amendment related to empowering a recognised association to make rules regarding grouping of members according to their functional interests, restricting voting rights, etc. The need for this amendment arose as it was found that the governing bodies (i.e. boards of directors) of most of the recognised associations were dominated by broker and commission agent-members while the genuine functionaries such as millers, stockists, crushers, ready dealers, etc., could not get adequate representation on the governing bodies in view of their numerical minority. It was, therefore, felt necessary to give increased weightage to these interests on the management of the recognised associations so that the speculative and non-speculative elements in the trade could be judiciously harmonised. Such increased weightage to the genuine interests could not be given in view of the provisions in the Companies Act under which these associations were incorporated. An amendment was, therefore, made to make an exception to the provisions in the Companies Act so that the members of the Association could be grouped into different panels in accordance with their functional interests and allotted seats on the governing bodies (boards) taking into account not only the numerical strength but also the functional importance of each group. The directors representing each panels were to be elected by members belonging to the respective panels.

(ii) Amendments in 1960

5. The second set of amendments made in 1960 was with a view to tighten the law for greater control over forward trading activities in the country and to remove certain doubts and difficulties that had come to the notice of the Commission in the light of the working of the Act till then. The salient features of the amendments made to the Act in 1960 were :

(i) **Definition of transferable specific delivery contract**—The definition of 'transferable specific delivery (tsd) contract' was amended so as to empower the Government to impose conditions relating to its transferability such as limiting the number of transfers etc.

(ii) **Functions of the Commission**—The original provisions in the Act relating to the functions of the Commission implied that the Commission was only an advisory body although actually it had to perform a number of executive functions such as giving directives to the recognised associations or taking action on its own in regard to the regulation of forward trading. Sub-sections (b) and (e) of section 4 of the Act were, therefore, amended so as to empower the Commission to keep forward markets under observation and to take such

action in relation to them as it may consider necessary and to inspect the accounts and documents not only of the associations but also of their members.

(iii) **Registration of all associations concerned with forward trading**—Under the scheme envisaged in the original Act neither the Government nor the Commission had any control on forward trading in commodities to which the provisions of the Act were not applied. In order to enable the Commission to keep a watch on the activities of the associations regulating or controlling forward trading in such free commodities, sections 14A and 14B were added. By these amendments every association concerned with the regulation and control of business relating to forward contracts was required to get itself registered with the Commission and to carry on such business under and in accordance with the conditions of a certificate of registration granted by the Commission. The object of these provisions was to enable the Commission to have a census of all such associations and to ascertain the extent to which such associations misused the ntsd contracts for speculative purposes in the commodities in which futures trading had been regulated or prohibited.

(iv) **Powers of a Civil Court to the Commission**—Under the Act, the Commission had substantial executive functions to perform. It received complaints from affected parties regarding various matters connected with the working of recognised associations, manipulation of markets by individuals acting separately or in concert and various types of illegal activities relating to forward trading and options. It had to enquire into such complaints and to take suitable action. Persons or the parties concerned were reluctant to furnish specific information or were prone to furnish incorrect information. In order to enable the Commissions to discharge this function effectively, section 4A was incorporated to give to the Commission the powers of a Civil Court under the Code of Civil Procedure while trying a suit, to summon and enforce the attendance of any person and examine him on oath, to require production of any document, receive evidence on affidavits, and requisition of any public record from any office.

(v) **Provisions for making contracts entered into in contravention of specified bye laws illegal**—The FC(R) Act required that the recognised associations should conduct trading in the commodities to which the regulatory provisions of the Act (i.e. section 15) had been applied, in accordance with the bye-laws framed for the purpose; but there was no provision in the Act to enable the authorities to take action against persons entering into forward contracts in contravention of the important bye-laws so framed. The result was that all forward contracts between members of recognised associations or with or through such members were legal, whether they were in accordance with the bye-laws, of the associations or not. A new provision was, therefore, incorporated which made the contracts entered into between, through or with the members of recognised associations in contravention of the specified bye-laws illegal. This provision enabled the Commission to require the recognised associations to incorporate in their bye-laws a provision for rendering the contracts entered into in violation of specified bye-laws, illegal. The important bye-laws specified for this purpose related to entering into contracts (i) above the maximum or below the minimum price prescribed for the purpose, or (ii) in futures deliveries for which permission of the Commission has not been granted to the recognised associations or (iii) on terms and conditions other than those provided in the bye-laws or (iv) beyond trading hours (i.e. kerb business) etc.

Sub-clause (h) was added to section 21 of the Act in order to penalise persons manipulating or attempting to manipulate prices of forward contracts in commodities regulated under section 15 of the Act.

(vi) **Presumptive provisions and burden of proof in respect of illegal trading**—Certain technical difficulties had been experienced in the course of prosecutions launched under the Act against the persons indulging in illegal forward trading. Even though the documents seized during the raid showed familiar types of entries pertaining to such trading, it could not be formally proved in the courts of law that they actually related to illegal forward trading. Further, the person or persons gathered at the premises raided with the obvious intention of entering into illegal forward trading, could not easily be made a subject of the charge as it was diffcult to prove their intention. Independent witnesses from the trading community were not forthcoming to prove the incriminating evidence in the seized documents due to reluctance to let down their counterparts in the trade. A provision was, therefore, made (section 22B) for shifting the burden of proof to the accused by providing that the books of accounts or documents containing entries making reference to quantity, quotations, rates, months of delivery, receipt or payment of differences or sale or purchase of goods or options in goods, etc. should be admitted in evidence without witnesses having to appear to prove the same and that such entries shall be **prima facie** evidence of the matters, transactions and accounts contained in the documents.

A provision was also made to the effect that if from any place the documents containing evidence of illegal contracts were found that place would be presumed to have been used and the persons found there would be presumed to be present there for the purpose of committing the offences under the Act.

(vii) **Provision for minimum fine and compulsory imprisonment :** Experience gained in the course of prosecutions launched under the Act had shown that the courts were reluctant to impose sufficiently deterrent fines or award imprisonment to the persons indulging in illegal trading. Such persons were let off lightly by the courts by imposing petty fines or awarding token imprisonment till the rising of the court, even though the offences committed by them were of a serious nature. Sections 20 and 21 were, therefore, amended for imposition of a minimum fine of Rs. 1000 in respect of the first offence and a compulsory imprisonment for the second and subsequent offences.

(viii) **Suspension of a member of recognised association**—A new section 12B was added empowering the Commission to suspend any member of a recognised association.

(iii) **Amendments in 1971**

6. The third set of amendments made in October 1971 (by an Ordinance dated 11th October, 1971 which was subsequently replaced by the Forward Contracts (Regulation) Amendment Act (Act No. 53 of 1971) was limited to the definitions of 'ready delivery contract' and 'forward contract'. Following the imposition of ban on futures trading in a large number of commodities and the progressive extension of this ban to ntsd contracts also in those commodities, habitual speculators started camouflaging their speculative activities in the guise of ready delivery contracts. The **modus operandi** adopted for the purpose was that the contracts were initially entered as ready delivery contracts for delivery within a period of 11 days from the date of entering into the contracts. No delivery of the goods was, however, actually given or taken against these contracts which were all settled by payment of differences between the rates of the original contracts and the rates of the off-setting contracts entered into, within a period of 11 days from the date of the original contracts. Often, after exchanging the differences, the contracts were re-entered at the settlement rate and this process was continued. No penal action could be taken against such speculative operations through the medium of ready contracts because the Commission was advised by the Attorney General of India that so long as the contract provided for delivery within a period of 11 days from the date of the contract, the contract would remain a ready delivery contract outside the purview of the Act and there was nothing in the Act which prohibited settlement by payment of differences without actual delivery. The use of ready delivery contracts for organising speculation in this manner assumed such a serious proportion that the Government at the instance of the Commission amended the definition of a ready delivery contract by passing an ordinance which provided that a contract which was performed by exchange of money difference between the contract rate and the settlement rate or clearing rate or the rate of any off-setting contract and as a result of which actual delivery of the goods against the contract or the payment of full price therefor was dispensed with would not be deemed to be a ready delivery contract but a forward contract as defined in the Act.

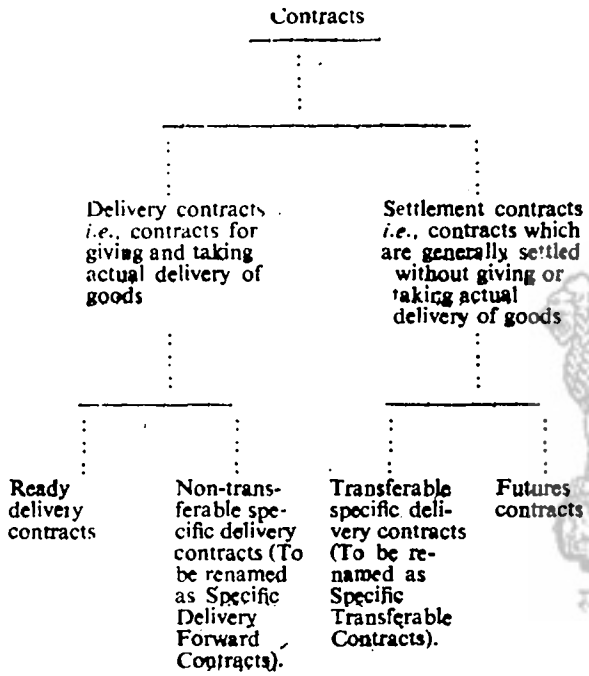
7. Similar amendment to the definition of ntsd contract was also immediately called for to clarify the definition and to prevent speculative trading in the name of these contracts. This, however, could not be done as the amendments in respect of forward contracts and related matters got tied up with the decision of the Government on the recommendations of the Review Committee which was appointed by the Government in February 1966 under the chairmanship of Prof. M.L. Dantwala.

Dantwala Committee's views on classification of contracts and their regulation

8. The Dantwala Committee, in its report submitted in October 1966, had, among other things, recommended certain basic changes in the FC(R) Act. One of its principal recommendations was that the classification of the different types of contracts under the

Act should be made with reference to (a) the purpose for which they are entered into, and the mechanics of their execution, and (b) not in terms of the timing of delivery against such contracts. In other words, the basic principle of the classification of contracts should be whether the contract is used primarily for giving and taking delivery of actual goods, or whether it is usually settled by payment of differences in prices and is used basically for purposes like hedging and speculation[1].

9. Dantwala Committee on the basis of this approach suggested the following scheme of classification of contracts :



10. The Committee, taking into account the nature of the delivery contracts and also certain facilities required by the genuine parties[2] to the so-called ntsd contracts, recommended that not only the ntsd contracts, should be called Specific Delivery (Forward) Contracts [SD (F) Contracts] but also that both ready delivery contracts and ntsd contracts (i.e. SD (F) Contracts) should be exempted from the regulatory provisions of the Act and that only the futures and the tsd contracts (to be renamed as specific transferable contracts) should be brought within the purview of the regulatory jurisdiction of the Commission. In accordance with its scheme, the Committee also recommended that the title of the Forward Contracts (Regulation) Act should be changed to the Futures Markets (Control) Act and that similarly the name of the Authority administering the Act should preferably be changed to the Futures Markets Commission instead of the Forward Markets Commission[3].

11. In other words, Dantwala Committee recommended the rejection of the earlier approach of the Expert Committee (Shroff Committee) (stated in paragraphs 11 and 12 of Chapter 3) on which the present scheme of the Act has been based and suggested an approach under which what have been called ntsd contracts in the present Act are not only not to remain completely non-transferable but, even after such modification, to be completely exempted from the purview of the Act. It says "we are aware that the permission to effect even a limited number of transfers under the ntsd may open the gate for speculation. This risk has to be taken, for, not to allow any transfer would be tantamount to making even a genuine and normal business practice illegal. The present legal provision, which does not permit any transfer, has inevitably led to the adoption of many dubious practices by the trade for the evasion of law and has given a lot of headache to both the Government and the Commission in trying to enforce the law".

Need to retain the present scheme of classification and regulation

12. We, however, feel that there is no need to change the present scheme of the classification of contracts or regulation. We have already pointed out in paragraph 13 of Chapter 3 that the experience relating to the enforcement of the FC(R) Act has clearly indicated that the approach adopted by the Expert Committee has proved to be broadly correct. While there is a case for amending the definition of ntsd contract given at present in the FC(R) Act to incorporate in its meaning certain facilities required by genuine trade functionaries, there is also a strong case in the light of actual experience of the Commission to make its definition precise and to provide for its regulation whenever necessary for ensuring that it is not used (1) for camouflaging speculative trading to evade ban or restrictions imposed by the Government on futures trading in the commodities, or (2) for acquiring pre-emptive hold on substantial quantity of future supplies of the goods concerned. We, therefore, recommend that the present approach adopted in the FC(R) Act of providing for the regulation of ntsd contracts whenever necessary should be retained instead of exempting these contracts from the scope of regulation altogether. We consider that certain amendments to the definition of ntsd contract and to various other provisions of the FC(R) Act, within the present framework of the Act, discussed hereafter are likely to make the Act a better instrument for regulating forward trading and checking illegal speculative activities.

Experience of Enforcement after 1960 amendments

13. The amendments made in 1960 enabled the Commission to regulate futures trading under the auspices of the recognised associations more effectively

[1]Paragraph 2.12 of the report of the Forward Markets Review Committee (Dantwala Committee).
[2]See paragraphs 30 & 31 of this chapter.
[3]See paragraphs 2.12 to 2.18 of the Report of Dantwala Committee.

as it could initiate disciplinary action against the members of recognised associations for violating regulatory measures either through the associations or on its own. More prosecutions could be launched due to the facility of presumptive provisions against persons indulging in illegal trading outside the recognised associations.

14. However, subsequently, particularly after 1965, due to emergence of several shortages in supplies and continuously rising trend in prices, futures trading in most of the commodities, in which such trading was regulated, came to be progressively banned by the Government or suspended by the Commission, on the suggestion of the Government, with the result that regulated futures trading in most of the commodities excepting a few such as jute goods, turmeric, pepper, came to a halt. Prohibition or suspension of futures trading in a large number of commodities gave rise to emergence of illegal futures trading on a very large scale at a number of centres throughout the country. The enforcement of the penal provisions of the FC(R) Act, therefore, became one of the major concerns of the Commission. During the course of several prosecutions launched thereafter certain glaring loopholes in the Act came to light.

Registered Associations

15. Important among these loopholes were in respect of the provisions relating to registered associations. The category of registered associations was created in 1960 under new sections 14A and 14B. Section 14A laid down that no association concerned with the regulation and control of business relating to forward contracts shall carry on such business except and in accordance with the conditions of a certificate of registration granted under the Act by the Commission. Section 14B required the Commission, on receipt of an application for registration, to make such enquiries as it considered necessary and grant a certificate of registration or refuse to grant it by order in writing. Under Rule 7A of the Forward Contracts (Regulation) Rules, 1954, the certificate of registration granted to an association under section 14B incorporated two conditions, viz., (i) that the association shall comply with such directives as may from time to time be given by the Forward Markets Commission, and (ii) that the association shall not conduct forward trading in any commodity other than those specified in the certificate except with the previous approval of the Forward Markets Commission.

16. The object of the amendment was to enable the Commission to have a census of all associations concerned with forward trading and to keep a watch on their activities. The working of these associations indicated that most of the associations were dens of illegal speculative trading mostly in banned commodities conducted either in the guise of trading in ntsd contracts in the banned commodities or futures contracts in the guise of the commodities to which sections 15 or 17 of the FC(R) Act had not been applied. Many of these associations went on challenging in the courts of law the powers of the Commission to restrict their trading activities to the commodities mentioned in their certificates of registration and continued to conduct speculative trading in the banned commodities in the guise of other commodities with impunity. It became extremely difficult to prove in the courts that the trading conducted was in banned commodities though intelligence reports from all sources indicated that the trading was actually in the banned commodities. After prolonged litigation involving a number of associations and the Government, the Supreme Court, by its judgement delivered in March 1975 (in Appeal No. 603(N) of 1973 Union of India and others v/s M/s. Rajdhani Grains Exchange Ltd., and others), upheld the right of the Commission to incorporate the above conditions. However, following this judgement, the persons organising such illegal trading devised a new **modus operandi** to continue their illegal activities. In order to circumvent the requirement of registration of an association the organisers of illegal trading started organising such trading without any formal organisation which could be identified as an association. The organisers called their contracts as party to party contracts in order to be able to defend that the contracts had ben entered into through personal negotiations and that they had not formed any association for the purpose of trading. The business was transacted by open bidding and recorded on printed contract forms which described the contracts as party to party contracts in a commodity to which the provisions of sections 15 or 17 had not been applied. When sections 15 or 17 was applied to the commodity concerned, the name of another suitable commodity was invoked. Even when the contract form contained such details as quantities traded, rates of purchases and sales, names of buyers and sellers, settlement of contracts by exchange of money differences, etc., prosecutions could not succeed as it was extremely difficult to prove that trading was actually in a banned commodity or that it was conducted under the auspices of an unregistered association. The parties concerned also often succeeded in forestalling any criminal proceedings against them by obtaining anticipatory stay orders from High Courts on the plea that they were conducting futures trading on party to party basis in commodities to which sections 15 or 17 had not been applied and which, therefore, did not attract any penal provisions of the Act.

17. Taking into account the various problems thrown up by the registered associations and large scale illegal futures trading through continuously changing devices, the Dantwala Committee had made three important recommendations viz., (i) the category of registered associations should be abolished[1]. (ii) the commodities in which futures trading is to be permitted should be listed in a schedule to be annexed to the new Futures Market Control Act, and futures trading in commodities other than those listed in the schedule should be declared illegal. The Government should however retain under the Act the right to add to or subtract from the list of the commodities in the schedule[2], and (iii) as a corollary of

[1]Paragraph 4.10 of the Report of Dantwala Committee.

[2]Paragraphs 6.8 and 6.9 and paragraph 2.19 of the report of Dantwala Committee.

(i) and (ii), trading in futures and in transferable specific delivery contracts (to be renamed as specific transferable contracts) should be permitted only under the associations recognised under the Act.

18. Though the Government ultimately did not take any decision on the Dantwala Committee's Report, while processing the Report the Government in the Ministry of Commerce (Department of Internal Trade), had referred the recommendations made at (i) and (ii) in paragraph 17 to the then Attorney General for advice. The Attorney General, however, opined that such a total ban on forward trading, as contemplated in the aforesaid recommendations, would not be constitutional vide his opinion reproduced below :—

> "To comply with Article 19(i) of the Constitution the general liberty to carry on forward trading should be recognised, subject to reasonable statutory restrictions in the interest of the general public, in relation to certain commodies regarding which the Government, on materials before it, consider that forward trading in such commodities would be detrimental to the interests of the general public."

Amendments to prevent illegal futures trading through camouflaging of commodities, etc.

19. We feel that in order to make the Act effective, it is necessary to prevent illegal forward trading in regulated or banned commodities (i.e. the commodities to which sections 15 or 17 have been applied) conducted in the guise of unregulated or unbanned commodities (i.e. the commodities to which sections 15 or 17 have not been applied). In view of the opinion of the Attorney General a total ban on ransferable or futures contract in all unregulated or unbanned commodities has to be ruled out. However, reasonable restrictions on trading through transferable or futures contracts can be provided in the public interest. Uncontrolled trading in transferable or futures contracts in any commodity can be harmful in many ways :

Firstly, such transactions, because of their transferable nature, are susceptible to speculation and manipulation which may cause sudden or unreasonable fluctuations in the prices of the concerned commodities detrimental to the producers, consumers and other interests.

Secondly, such contracts, when uncontrolled, may affect adversely the interests of stockists, dealers, millers, exporters and all others engaged in handling the commodities if they use them for hedging against possible loss through fluctuations in prices or through their influence on the prices of the commodities even if they do not use them.

Thirdly, when transactions in these contracts are on large scale and those who are handling the actual commodity are also involved in them, the prices of these transactions get disseminated throughout the country and form the basis for determining the market prices to the producers and the consumers of the commodities and thus influence the movements of the commodities in the country.

20. Moreover, most of the transferable and futures contracts are readily transferred by the sellers and the buyers and settled by payment of money differences. Even in the case of transferable specific delivery contracts, though the two parties which finally remain seller and buyer are required to give and take delivery of the goods, all other parties to the contracts settle the contracts by payment of differences. It is, therefore, inherent in the nature of these contracts, involving in any case more than two and often a number of parties, that orderly facilities in them could be provided only under the auspices of an association with comprehensive rules and regulations, if (i) a tract of all the parties to the contract is to be kept, (ii) payment of money differences on the basis of price fluctuation is to be arranged and defaults, if any, are to be dealt with, (iii) arbitration and survey machinery to settle disputes is to be made available, and (iv) fair and impartial final settlement to all concerned is to be arrived at.

21. Taking into account these various aspects of trading in transferable contracts, we consider that their misuse for illegal futures trading can be prevented by providing that (i) all trading in transferable contracts (i.e. forward contracts other than ntsd contracts) which is not regulated or controlled by an association shall be illegal; and (ii) no association regulating and controlling transferable contracts shall do so without obtaining a certificate of recognition from the Central Government except when the Central Government has specifically exempted any commodity from this requirement of recognition.

22. The net effect of these two provisions in the Act would be that trading in all transferable contracts (and in ntsd contracts when such trading is specifically regulated) will be under the auspices of recognised associations only and there will be no need for a separate category of registered associations. The possibility of conducting illegal futures trading in the name of so-called party to party contracts would thus be eliminated. Every association desirous of organising trading in transferable contracts would be required to make an application to the Central Government for grant of recognition to organise such trading. The Forward Markets Commission on behalf of the Central Government would then be in a position to make such enquiry as may be considered necessary. The decision of the Government whether to permit such trading under any recognised association or not to permit it would be taken only after the Government have applied their mind to the issue on

the basis of the material before it. In our view, these restrictions cannot be construed as unreasonable. We, therefore, recommend the amendment of the Act as suggested in Paragraph 21 above.

Other amendments necessary to the Act

23. A number of other amendments to the various provisions of the FC(R) Act also appear necessary in the light of the difficulties experienced by the Commission and certain loopholes that have come to light since the amendments made in 1960.

24. The difficulties brought to our notice by the Commission are of two types (i) legal and (ii) practical.

24.1 The legal difficulties of the Commission arise mainly from inadequate provisions in the FC(R) Act. Thus for example, the definition of an ntsd contract meant for actual delivery neither requires the performance of such contracts by actual delivery nor is there any provision in the Act to penalise persons performing these contracts otherwise than by actual delivery. Similarly, the presumption under section 22B of the Act is not available where a raid has to be conducted without obtaining a warrant in view of the wording of section 22A. Thus in a large number of cases, where raids have to be organised at a very short notice without obtaining warrant, the presumption becomes unavailable and the cases fail in courts of law.

24.2 So far as the practical difficulties are concerned, the Commission has pointed out that sophisticated techniques are adopted by unscrupulous elements in the trade in the light of the experience gained by them during the course of prosecutions launched under the Act. These elements no longer maintain any regular books of accounts but only loose slips of paper on which only minimum and codified entries are jotted down from which it is difficult to prove in a court of law that they pertain to illegal transactions as vital details such as the name of the commodity, delivery month, differences settled, etc., are not mentioned. Large volume of business is transacted over intercom and privately connected and battery-operated phones and profit and losses arising from such business are exchanged in cash often in unaccounted money.

Amendments suggested by the Commission

25. Taking into account all these factors, the Commission had in October 1978 proposed a number of amendments to the FC(R) Act which are given in Annexure XV. These amendments had been cleared by the Ministry of Law, Delhi. However, since thereafter the Government appointed this Committee to go into the various aspects of forward trading including amendments necessary to the FC(R) Act, the Government have referred these amendments to us. The amendments suggested by the Commission broadly fall into two parts, the first part consisting of core amendments which are considered absolutely essential by the Forward Markets Commission and the second part consisting of amendments to confer additional powers on the Commission for more effective and speedy enforcement of the penal provisions of the Act.

26. In the first part, amendments have been proposed mainly under four categories viz., (a) definitions in the Act, (b) provision relating to registered associations, (c) amendments to tighten the penal provisions in the Act, and (d) amendments to fill certain lacunae in the existing Act.

(a) **Amendments to definitions**

27. The amendments to definitions mainly relate to the definitions of ntsd contract and ready contract.

(i) **Definition of ntsd contract**

28. The ntsd contracts are meant to be used for normal marketing of goods over time. With the object of ensuring actual delivery of goods against these contracts, the definition of the ntsd contract prohibits transfer of rights or liabilities under the contract or under documents of title relating to it such as delivery order, railway receipt, bill of lading, warehouse receipt, etc. The main loopholes in this definition that came to light in the course of prosecutions launched in the various courts and the legal opinions obtained were (i) the prohibition on mere ransfer of documents of title did not ensure actual delivery as it was possible for two parties to enter into mutually offsetting ntsd contracts and dispense with the requirement of delivery altogether, (ii) the definition could be construed to mean that it was enough if the contract **'provided'** for delivery at the time of entering into the contract and need not necessarily result in delivery, and (iii) the absence of any penal provision in the Act for the performance of ntsd contract otherwise than by actual delivery of the goods.

29. These loopholes are proposed to be plugged by suggesting an amendment to the present definition of ntsd contract to provide that an ntsd contract performed by exchange of money difference between the contract rate and the settlement rate or the clearing rate or the rate of offsetting contract as a result of which the actual delivery of goods is dispensed with shall not be deemed to be an ntsd contract. This approach to the definition of ntsd contract is similar to that adopted in respect of the amendment already made to the definition of ready delivery contract for plugging similar loopholes.

30. It had also been brought to the notice of the Commission that the practices and procedures adopted for entering into ready and ntsd contracts need to be taken into account while defining these two types of contracts. Many of the buyers in the terminal markets make purchases in the upcountry markets through their commission agents at such upcountry centres. These purchases are generally made on 'pucca adat' (i.e. principal to principal) basis from the commission agents. The commission agents, in turn, purchase the goods from the local merchants. There is no

privity of contract between the terminal buyer and the up-country merchant and the comminal agent is responsible to both the parties for the performance of the contract. In all such cases, at the time of delivery of goods, the railway receipt (or any other document of title to goods) pertaining to the contract is sent by the upcountry seller in the name of the commission agent who endorses it to the ultimate buyer in the terminal market. In such cases delivery of goods is given by the upcountry seller to the terminal buyer and the railway receipt is passed on by the upcountry seller first to the commission agent who endorses it in favour of the terminal buyer. Again in consignment transactions, the upcountry seller generally sends his document of title to the buyer through a bank. In such cases bill of exchange is drawn on the buyer but the document of title e.g. the railway receipt, is endorsed in favour of the bank as a collateral security so that the seller is in a position to get an advance from the bank against his sale. The bill of exchange is presented by the bank to the buyer for payment or acceptance but if the bank has no office at the place where the bill is to be presented, the bank endorses the document in favour of its 'correspondent' bank which then transfers the rights under the document to the buyer on payment or acceptance of the bill. If these endorsements of documents by the commission agents or banks were to be counted as 'transfers' then many genuine ready and ntsd contracts could be interpreted as transferable contracts, could attract the penal provisions of the Act and result in harassment to the trade.

31. These were genuine fears and in view of this, while plugging the loopholes in the definition of 'ready delivery contract' in 1971 to prevent its use for camouflaging speculative trading, opportunity was taken to incorporate these requirements of the genuine trade and the amended definition of ready delivery contract now provides for these facilities for entering into such contracts. The need for similar facilities for ntsd contracts is all the more since these are contracts of longer duration. However, as indicated earlier, the question of amending the definition of ntsd contract was linked with the question of other amendments to the FC(R) Act and was postponed as no decision was taken on the recommendations of the Dantwala Committee which had also recognised the need for these facilities. The amendment suggested by the Commission to the definition of ntsd contract for plugging the loopholes mentioned in paragraph 28 of this chapter also takes into account the need for these facilities.

(ii) **Amendment to the definition of ready delivery contract**

32. Although the definition of a ready delivery contract was amended in 1971, the Commission has proposed a few amendments to make the definition technically correct and remove certain defects. The present definition of ready delivery contract requires not only the completion of delivery of goods but also the payment of a price therefor within a period of 11 days. The need for the provision for completion of actual delivery within 11 days is evident but the insistence on the completion of payment therefor within that period is impracticable. Even small consumers purchasing their monthly provisions from grocers by taking delivery across the counter make payment often after eleven days. Such credit facility does not make a contract speculative. At the same time, there are some contracts where delivery is made immediately or within 11 days but the price is fixed at a later date by mutual consent on the basis of the view taken of expected price situation (e.g. Jangad contracts in Gujarat). Such contracts are inherently speculative in nature and, therefore, should not be treated as ready delivery contracts. The amendments proposed to the definition of ready delivery contract eliminate the requirement of the completion of the payment for the delivered goods within 11 days after the date of the contract but require the parties to the contract to fix the price at the time of entering into the contract.

33. The Commission as well as the Committee had received representations to the effect that the period for giving and taking delivery against ready delivery contracts should be extended beyond 11 days to about 30 days on account of factors such as transport difficulties, non-availability of railway wagons, etc. The Commission in its proposed amendment has not suggested any extension of this period. We also do not consider such extension necessary. We feel that this demand has been put forward mainly on account of complete ban on non-transferable specific delivery contracts (i.e. contracts of duration longer than 11 days) in many of the commodities to prevent their use for speculative purposes. Any extension of the duration of ready delivery contract will tempt speculators to use ready contracts for speculative purpose by various ways despite the amended definition. Moreover, such an extension would not be necessary if the recommendations made by us relating to ntsd contracts in another Chapter were accepted. We, therefore, recommend that the duration of 11 days after the date of the contract prescribed for the completion of delivery of goods in the present definition of ready delivery contract need not be extended.

(iii) **Amendments to other definitions**

34. The Commission has proposed amendments to the term 'association' on account of the difficulties experienced by it in taking action against illegal trading organised not under a regular 'association' but under some loose organisation which cannot be identified as an 'association'. The persons conducting such trading claim that they have not constituted an association within the meaning of the term 'association' as defined in the FC(R) Act. The scope of the definition of the term 'association' is, therefore, being proposed to be widened so as to cover loose types of organisations formed by individuals or groups of individuals.

(b) **Matters relating to registration**

35. The definition of the expression 'registered association' has also been likewise proposed to be amended

by the Commission on the lines of the existing definition of a recognised association so that registration would be commodity-wise and according to the type of the contract and not remain general as at present. Along with the amendment to the definition, the Commission at suitable places has suggested amendments to provide for withdrawal of registration and suitable penalties against organisers of non-registered associations or registered associations conducting trading in violation of the conditions in their Certificate of Registration.

36. It may be pointed out that the proposed amendments in respect of the terms viz., 'association' and 'registered association' and other related matters would not be necessary if our recommendations contained in paragraph 21 of this Chapter were accepted and given effect to as, in that case, the category of registered associations would stand abolished. The amendments proposed by the Commission would, however, be necessary if these recommendations are not accepted.

(c) **Amendments to tighten penal provisions**

37. The object of the remaining core amendments proposed by the Commission is to tighten the penal provisions of the FC(R) Act. These amendments take into account the various recommendations made in this behalf by the Law Commission in its 47th Report as well as the Commission's own experience in the course of prosecutions launched under the Act. The trying courts generally took a lenient view of the offences committed under the Act and rarely imposed a fine in excess of the minimum amount of Rs. 1,000 prescribed for the first offence. In fact in some cases the courts did not impose even the minimum fine and awarded a token imprisonment till the rising of the court or merely administered to the accused a warning under the Probation of Offenders Act. The proposed amendments provide for (i) a mandatory minimum imprisonment of six months and mandatory fine of Rs. 3000 for the first offence, (ii) increase in the period of maximum imprisonment from one year to three years for the first offence both under sections 20 and 21 (iii) increase in the compulsory imprisonment for the second offence both under sections 20 and 21 of the Act from one month to one year and the minimum fine from Rs. 1000 to Rs. 5000 and (iv) increase in the maximum imprisonment for the second offence from one year to seven years both under sections 20 and 21. The proposed amendments also remove the discretion conferred on the magistrates to release the offenders by taking recourse to the provisions of the Probation of Offenders Act and empower them to impose a fine in excess of the present limit of Rs. 5000 laid down in the Cr. P. C.

(d) **Amendments to cover certain lacunae**

38. The amendments proposed by the Commission to remedy certain lacunae in the existing Act include (i) a new section 4-C to provide for usual safeguards to meet difficulties that may arise from situations such as any vacancy or technical defect in the constitution of the Commission, (ii) power to impose fine on members of recognised associations in case their suspension from membership, which has already been provided for in the existing Act, is not considered necessary, (iii) amendments in the penal provisions under section 21 to make presumption under section 22B(2) available in the case of option trading also, (iv) amendment to section 22B(1) to make presumption under section 22B applicable to seizures effected both with or without a warrant and (v) reference to section 17 in the proviso to section 18(1) which is an omission.

Powers for search and seizure

39. The second part of the amendment proposed by the Commission is mainly to enable it to discharge its responsibilities of checking illegal forward trading more effectively and seeks powers to it for search and seizure which at present are vested only in the State Police Officers. The Commission has proposed a new provision in the Act under which it could authorise any of its officers not below the rank prescribed in the Act to search and seize documents from any place where he suspects that illegal forward trading is taking place or that the documents pertaining to such trading are being secreted. These powers have been proposed by the Commission for its officers on the condition that adequate increase in the staff suitable for the purpose is sanctioned by the Government for the Head Office and for different regional offices that would have to be set up for the purpose.

40. Prosecution of offences under the FC(R) Act is based mainly on the documentary evidence collected from the premises used for and the persons indulging in illegal forward trading. The powers for search and seizure of such documentary evidence are, therefore, the most important instruments of enforcement action. At present seizure of documents can be effected only by the police authorities by virtue of powers derived by them under the Criminal Procedure Code in respect of offences made congnizable under section 23 of the FC(R) Act or on authorisation of warrant by a Presidency Magistrate or a Magistrate of the Ist Class as laid down under section 22A of the Act. The general powers for search and seizure contained in the Criminal Procedure Code are restrictive in nature, either by reason of class of officers who can exercise these powers or by conditions precedent required before powers can be exercised. Under the FC(R) Rules, the Commission like any other citizen is merely expected only to communicate the information about illegal forward trading to the police. even the Director of Enforcement of the Commission, though a Senior Police Officer of the I.P.S., has no powers for search and seizure.

41. The Commission has contended that its dependence on the police authorities for search and seizure often comes in the way of successful enforcement action on account of the following reasons :—

(i) Due to the technical nature of the offences under the FC(R) Act, the task of collection

of information about illegal forward trading and its verification has to be borne by the officers of the Commission who have the necessary expertise in the matter. As the Commission's officers have no powers for search and seizure they have, after verification of information, first to approach the police authorities for organising the raid. As a result, quick and surprise action is not possible. Very often, the police authorities are pre-occupied with more urgent problems of law and order and action has, therefore, to be postponed. Loss of time results in leakage of information about the possible raid to the parties concerned who, being alerted, remove the documents from the premises.

(ii) On the basis of the information contained in the documents seized from one party, follow-up action has to be taken against the opposite parties who have transacted illegal forward business with the party raided. Quick follow-up action against such opposite parties located at distant centres is not possible as the concerned police authorities have their jurisdiction limited to one centre only.

(iii) When simultaneous raids have to be conducted at a number of centres in different States, co-ordination of action through police authorities located in different States becomes difficult.

(iv). The approach of the police personnel, often in uniform to the venue of raids, alerts the parties concerned who succeed in destroying the documentary evidence in their possession before the premises are searched.

(v) If powers for search and seizure are given to the officers of the Commission, the present Enforcement Directorate of the Commission can become a self-sufficient unit for taking actions against illegal forward trading.

(vi) Provisions for search and seizure by departments concerned have been made in other Acts like Foreign Exchange Regulation Act, Income tax Act, Essential Commodities Act, etc. The Law Commission of India, in its Report on Trial and Punishment of Social and Economic Offences, have also recommended more liberal provisions as to search and seizure on the lines of section 19(D) of the Foreign Exchange Regulation Act.

(vii) In order that powers for earch and seizure are not abused by the officers of the Commission, suitable provisions can be made so that only such officers of the Commission as are authorised by the Commission would have the powers for search and seizure.

42. The Ministry of Law, Delhi, to whom all the amendments suggested by the Commission were referred, have conveyed that they have no objection to these amendments.

43. We have carefully considered these proposals made by the Commission to the Government. We consider these to be reasonable and essential except the proposal relating to search and seizure discussed in paragraphs 39 to 41. Having regard to the nature and strength of the staff available at the disposal of the Commission, we do not think that the proposal would be practical. First, excepting the Director of Enforcement, who is a police officer on deputation from the State Government, none of the existing officers of the Commission is, by training and temperament, equipped to deal with the task of conducting searches, procuring witnesses, etc. These officers have been recruited initially for a different type of work altogether viz.; research and regulation on forward markets. Secondly, it is quite likely that once the power for search and seizure are vested in the officers of the Commission, the local police authorities may no longer consider themselves solely responsible for investigation of the offences under the FC(R) Act and their full cooperation may not be easily forthcoming. Thirdly, enforcement action often involves deployment of a large force to effect seizures from number of premises and persons suspected to be indulging in illegal forward trading. We doubt whether the Commission would be in a position to spare sufficient staff for the purpose. Fourthly, unlike the Income-tax or Customs Departments, which have been given powers for search and seizure, the Commission does not have a wide network of local offices and branches all over the country to reach every nook and corner of the country where illegal forward trading is being conducted. Finally, the officers of the Commission may not get the information and cooperation that local police may get. We are, therefore, of the opinion that the powers for search and seizure may not be vested in the Commission's officers whose role should be limited, as at present, only to rendering technical assistance to the police authorities in the seizure of documents and their scrutiny with a view to giving expert opinion on the nature of contracts contained in them.

Adjudication of the offences under the FC(R) Act

44. The Commission, we understand, had as early as in 1969, made a proposal to the Ministry for departmental adjudication of the offences committed under the Act. Briefly, the proposal was that the Director of Enforcement of the Commission would have the powers to adjudicate offences under the Act departmentally by imposing fines with an option to refer any of such offences to the Court of Law for regular trial if he was of the opinion that the penalty in the form of fine would not be adequate. The scheme also provided for an appeal to the Commission against the decision of the Director in regard to the penalty imposed. The scheme of penalty by way of fine only

was related to the values of the illegal contracts and profits made therefrom. It was proposed that the penalty in the form of fine for the first offence would be 5% of the value of the contracts in respect of which the contravention had taken place plus 2½ times the total amount of profit on the contracts or Rs. 1000 whichever was more and for the second and subsequent offience, the penalty was 10% of the value of the contracts plus 5 times the total amount of profits on forward contracts or Rs. 2000 whichever was more. The Government have yet to take decision on these proposals of the Commission.

Compounding of offences as alternative to adjudication

45. We have considered this proposal of the Commission. Adjudication involves setting up of a cumbersome and costly machinery which will have to be independent of the Director of Enforcement of the Commission. It would also be necessary to set up an Appellate Tribunal consisting of atleast two members with adequate judicial background and expertise in technicalities of forward trading. Looking at the limited number of cases made out under the FC(R) Act, it appears to us that the adjudication machinery will have to remain idle for most of the time. We would, therefore, instead suggest that a provision may be made in the FC(R) Act providing for compounding of offences under the Act with the sanction of the Commission, on the lines of provisions made in section 279(2) of the Income-tax Act. This would enable the Commission to get quick disposal of a large number of cases which drag on for long time in law courts and at the same time, proceed with prosecution in those cases which, on the basis of evidence on record, are considered sufficiently strong by the Commission for security conviction.

46. We would like to point out that the discretion to the Commission to compound the offences under the FC(R) Act, as proposed by us, would not be unfettered. Since the prosecutions under the FC(R) Act are launched by the State Government/Union Territories only, it would be necessary for the Commission to consult the State/Central Governments for laying down general guide lines to be followed to ensure that the powers for compounding are exercised in a uniform and judical manner throughout the country. We, therefore, recommend that the offences under the Act, should be made compoundable with the sanction of the Forward Markets Commission.

Other Amendments

47. A few more amendments would also be necessary to implement the proposals made by us in Chapter 5 on 'Basic Requisites for Regulation of Futures Trading'. These are summarised below :—

(i) Amendment empowering the Commission to require all non-members desirous of trading in futures markets to register themselves with the Commission through the concerned recognised associations subject to rules and conditions prescribed by the Commission.

(ii) Amendments empowering the Commission to require all operators, members as well as non-members, to submit periodical returns to the Commission directly showing the volume of trading and break-up of the open position as hedge and speculative as defined by the Commission in each market and in each delivery separately.

(iii) Amendments requiring all business of non-members to be put through the trading ring of the recognised association by public outcry, and

(iv) Amendments empowering the Commission to require each member of a recognised association to obtain a minimum margin or deposit from a non-member client as a percentage of the value of the goods and requiring each of such member not to commingle the margin or the deposit amounts so received with his own funds for use of any personal purpose but to hold it in segregation.

CHAPTER 8

STRENGTHENING OF THE FORWARD MARKETS COMMISSION

We have in the previous Chapters explained the nature of futures trading, the commodities in which it may be permitted under present conditions and suggested certain amendments to the FC(R) Act to make regulation economically and socially more beneficial and for efficient enforcement of the Act to check illegal forward trading. If the recommendations of the Committee in respect of these matters are accepted by the Government, it would substantially enlarge the role of the Commission. In this Chapter we have considered the implications of this enlarged role with regard to the status and staff requirements of the Commission.

2. The Committee feels that the existing provision in the FC(R) Act regarding the strength of the Members of the Commission is quite adequate. Sub-section (2) of section 3 of the FC(R) Act, as amended in 1960, provides that the Commission shall consist of not less than two but not exceeding four Members one of them nominated by the Central Government to be the Chairman thereof. The Committee, however, notes that two posts out of four have remained unfilled for long. It is necessary that the vacant posts be filled so that a better division of labour regionally, functionally and commodity-wise and better handling of the volume of work can be brought about. As the Commission has to deal with persons and agencies of the highest standing in trade, commerce and manufacture, it is important that the official standing of its Members and Chairman should be of a high level. It is, therefore, recommended that the Chairman of the Commission be given the status of an Additional Secretary and the Members of a Joint Secretary in the Central Government.

3. At present the office of the Forward Markets Commission is divided into three broad divisions viz., (i) Commodity Division, (ii) Enforcement Division & (iii) Administration Division. Duties assigned to these divisions are briefly stated below :

(i) **The Commodity Division** aids the commission in the discharge of the various statutory functions. Equipped with a specialised staff, manned at the senior and junior officers' levels by I.E.S. personnel, it conducts inter alia studies into the economics of commodities, examines the need for permitting or banning forward trading under the provisions of the Act, analyses returns received from members of recognised associations to keep their activities under surveillance, maintains a close watch on the price trends and other developments in the market and suggests suitable remedial measures. Senior officers of this Division are nominated by the Central Government as Directors on the Boards of Directors of recognised associations, in pursuance of section 6(2) (b) of the FC(R) Act, to represent the Central Government. They attend Board meetings of the recognised associations periodically, watch their functioning and keep the Commission informed.

(ii) **The Enforcement Division** enquires into complaints regarding illegal forward trading, assists the local police in organising raids at centres where illegal forward trading may be taking place, scrutinises the books and documents seized in such raids and assists the various State Governments in launching prosecutions against the offenders. This division also organises periodical training courses for police officers from the various States to educate them on the enforcement aspects of the FC(R) Act. During such training, the nature of the offences involved, the **modus operandi** adopted by the trade, uptodate case laws on the subject and other relevant aspects are explained to them.

(iii) **The Administration Division** provides the necessary secretarial assistance to the Commodity and Enforcement Divisions and looks after the establishment including house keeping, budgeting, cash and audit, and also department accounting.

4. We feel that the staff strength of both the Commodity and Enforcement Divisions of the Commission will have to be appropriately strengthened in the light of our various recommendations to enable the Commission to discharge its functions more comprehensively and efficiently. We have recommended resumption of futures trading in a few commodities and regulation of trading in ntsd contracts in important commodities. If the Government accepts these recommendations, the number of recognised associations to be looked after by the Commission would, no doubt, increase considerably.

Regional Offices

5. As pointed out in paragraphs 21 and 22 of Chapter 3 although the role of the Commission under the FC(R) Act regarding illegal forward trading is confined to communication of information in respect of such trading to the authorities and rendering them expert advice, in actual practice the Commission has to play a major role in the task of prevention of illegal forward trading. The nature and composition of the Enforcement Directorate set up by the Commission for this purpose and the various functions

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performed by it have been described in paragraphs 20 to 26 of Chapter 3 of this Report. However, having regard to the selective approach towards futures trading which we have recommended, the magnitude of illegal forward trading in the country and the potential for anti-social elements devising ingenious methods to conceal such trading, we feel that the present enforcement arrangements in the office of the Commission are totally inadequate to cope with the task of combating illegal forward trading.

6. During the meeting of the D.I.Gs (C.I.D) of the States, convened by the C.B.I., as early as in 1965, many of the D.I.Gs had complained of the lack of adequate assistance to them by the Enforcement Directorate of the Commission in tackling the problem of illegal forward trading and suggested that the services of a large number of experts should be made available to them for the purpose. Some of the I.G.Ps of the States like U.P. had also recommended that Regional Offices of the Commission should be set up in their States. The Commission itself had also made proposals in the past for setting up Regional Offices at places like Delhi. The major pockets of illegal trading are located in the States of Gujarat, Rajasthan, Punjab, Haryana, Uttar Pradesh and Madhya Pradesh and the Union Territory of Delhi and the Cities of Bombay and Calcutta.

7. Taking into account these requirements, we recommend as follows :

> Regional Offices of the Commission may be established, in addition to the one already at Calcutta, at Delhi, Ahmedabad and Lucknow to begin with. These offices should be under the charge of a Gazetted Officer who should be assisted by supporting staff at the level of Senior/Junior Research Assistants and necessary subordinate staff. The total strength of each of the Regional Office may vary according to the requirements of the region. These Regional Offices would be in a position to collect information relating to illegal forward trading in the respective regions and render timely and effective assistance to the local police authorities in taking enforcement action. They would also be required to collect and forward to the Commission economic data relating to the concerned commodities in the region and co-ordinate the work relating to the regulation of trading at the recognised associations in the region as may be directed by the Commission from time to time. The establishment of such small Regional Offices would be feasible economically and assist in the efficient discharge of the responsibilities of the Commission under the FC(R) Act.

Research unit

8. There is no regular research unit manned with staff having adequate statistical and econometric qualifications in the office of the Commission to undertake specialised studies except some staff assisted by a few computors engaged for the tabulation and simple analysis of the data. Further, the present system for reporting trading details is also not comprehensive. We have recommended a statutory return requiring the operators to show separately their hedge and speculative positions and such other details as the Commission may consider necessary from time to time. On the basis of the returns, price data and other details obtained from various sources, the Commission should undertake research activities which should cover, among other things, (i) extent of the use of recognised futures markets for hedging and speculation, (ii) effectiveness of the regulatory policies of the recognised associations and the Commisson to facilitate hedging and curb excessive speculation, (iii) the relationship between ready and futures prices, factors responsible for distortions, if any, in such relationship and the effect of such relationship on hedging and speculation in the market, (iv) the correctness or otherwise of futures prices as forecasts or as indicators of the future trend of prices, (v) the effect of futures trading in the commodity on the extent of fluctuations in ready prices of a commodity, etc. We have listed only a few fields in which research studies could be undertaken. The list is illustrative and not exhaustive. The potential for such research studies in respect of futures market is quite wide as is evident from the studies published by the Commodity Exchange Authority in the U.S.A. and other countries.

9. The timely publication of the data regarding volume of trading, open position, ready and futures prices and studies regarding the functioning of the recognised futures markets in the Forward Markets Bulletin brought out by the Commission would be of much help to the Government in framing its policies and also to the trading community in adopting a responsible approach towards futures trading.

CHAPTER 9

SUMMARY OF CONCLUSIONS AND RECOMMENDATIONS

Approach to futures trading

The Committee first addressed itself to the task of laying down its approach to futures trading in the light of the prevailing economic conditions and marketing and distribution system prevailing in various commodities.

2. It noted that not all commodities are fit for futures trading. A commodity to be eligible for futures trading must be homogeneous, capable of being standardised in one or more grades and its supply and demand should be so large that even the biggest purchase and sale of the largest speculators constitute a fraction of the total market. It should be free from substantial control either by a Governmental or public authority or a private organisation, cartel, association, corporation or individual. Its supply and demand should be uncertain and it should neither be a perishable commodity nor subject to changes in style and fashions. Lastly, leading segments of the production and trade sectors handling the commodity and prepared to use it for hedging should come forward to organise futures market.

(1.2 to 1.8)

3. While it is a necessary condition for a satisfactory operation of futures markets that supply and demand should be large, the Committee noted that in India—unlike the major cereals, in particular, wheat, and cotton which have undergone a substantial technological change—other foodgrains, especially the inferior foodgrains and almost all industrial raw materials produced in agriculture have been stagnating owing to lack of technological breakthrough. As more resources are bound to be concentrated in these commodities in the future, supplies are most likely to respond to growth in demands, and the markets for almost all agricultural commodities, except cereals, and in particular inferior cereals, are bound to grow. Indian conditions are most likely to become more and more favourable for forward trading in these commodities as a result of the expansion of the volumes of demands and supplies. In the case of most of these agricultural commodities almost the entire production is for marketing. The expansion of the market size generally goes with improvement in market sophistications which would also be a favourable circumstance for the operation of futures market.

(1.10 and 1.11)

4. As regards the existing marketing and distribution system in commodities, the position is that in rice and wheat and some other foodgrains, there is a complex system of regulation and control involving support prices, procurement and a vast net-work of public distribution agencies. This social necessity involves the Government in a complex and costly distributive apparatus which ties up a great deal of Governmental resources. These mechanisms cannot be extended for commodities other than the most urgent ones. In this context the question arises as to what other methods could be used to regulate the prices of these other commodities, many of which exhibit a high degree of price fluctuations. The Committee is of the opinion that in such a context futures trading can be considered as a possible measure, in suitable cases, for dampening the peaks and lifting up the valleys of prices; in fact, in some cases, such a measure may turn out to be a necessity.

(1.12 and 1.13)

5. As for the benefit of futures trading to producers and consumers, the Committee's considered view is that if the gains from futures trading accrued only to those who traded in the futures market and to nobody else, or indeed, if the gains to futures traders were accompanied by losses to producers, manufacturers, consumers and other social interests, this Committee would not recommend resort to futures trading at all. However, futures trading, under suitable conditions and when properly regulated, can be of immense help to growers and various other functionaries.

(1.14)

6. The cultivators who grow commodities in very large quantities can use futures markets for hedging their crops or stocks. This enables them to spread out the sales of such stocks over a period and obtain a better price for their produce. Even if the cultivators do not participate in the futures markets directly, such markets are beneficial to them as an advance indicator of the expected levels of prices during the marketing period, enabling them to undertake proper crop planning. In the absence of futures market in appropriate commodities, the traders and manufacturers attempts to cover their risks by charging a higher price to the consumers or by paying a lower price to the producers. In other words, the margin between what the producer receives and what the consumer pays is widened just because no adequate method to cover risks of traders and manufacturers is provided. It is obvious that in the absence of futures trading and risk minimisations, as the farmer gets less, his motivation to produce more and,

Note : In the references given in brackets below conclusions/recommendations, the first number refers to the Chapter number and the second number to the paragraph number.

indeed, his investment capability gets reduced. On the other side, in the absence of futures trading, as the consumer pays more, demands may get constrained and the final retail market does not get widened as it would when, in appropriate cases, futures trading exists. Thus futures trading, in appropriate cases and suitable conditions, makes the return to the producers higher and the price to the consumer lower.

(2.27, 2.28 and 1.16)

7. As regards the role of futures trading in promoting exports, the Committee has come to the conclusion that hedging facility is of invaluable help to exporters. It enables them to make hedge purchases against the overseas sale contracts. Besides, the futures markets supply quotations for different future delivery periods based on the expert assessment of the anticipated future supply and demand which enables them to quote to foreign buyers, for different shipment periods. Further, being assured of normal profits because of the insurance service provided by the futures market, the exporters are in a position to trade on a smaller margin of profit which increases their competitive capacity in the world markets. Furtures markets can, therefore, be considered as one of the instruments of export promotion.

(2.30 and 2.31)

8. There is no scope for futures trading in any commodity if there is complete control of the State on its supply and distribution. However, if the private trade is free to procure a large part of the supply and handle its marketing or if the State procures entire supply from producers but sells it to the private trade for its distribution, the trade interests would need hedging facilities. Under the price support programme, the State or its agencies are committed to purchasing the commodity when the price of the commodity tends to fall below the prescribed support prices. Futures trading is not incompatible with such programme because there is considerable scope for determination of fair competitive prices above these minimum levels and there is no reason to deprive the farmers of such higher prices. Similarly, buffer stock schemes are also not incompatible with futures trading if the major part of the crop is to be marketed by the private trade. In fact, the existence of futures markets in commodities in which management schemes have been introduced will be helpful to the proper implementation of the schemes, since the agencies operating the schemes have generally to face the same problems, as faced by the private trade, in the management of the stocks procured by them. The availability of futures prices would also enable them to decide their buying and selling policies and the quantum of stocks to be held.

(2.33, 2.34 and 2.35)

Commodities suitable for futures trading

9. The Committee has considered the desirability of permitting futures trading in different commodities under present conditions. The commodities considered for this purpose are those in which there has been a tradition of futures trading and in some of which such trading has been suspended from time to time and also those commodities in which there has been a demand for introducing futures trading. Our conclusions and recommendations in respect of various commodities are as follows :

(4.1)

(i) **Foodgrains—Cereals and Pulses**

Foodgrains being commodities of mass consumption have been subjected, for very good social and economic reasons, to fairly thorough regulations and controls through such measures as support price fixing, retail price fixing, procurement, buffer stock operations and organisation of ration shops in an extensive public distribution system. As our criteria have shown, such commodities cannot be a fit material for trading in the futures markets. The Committee, therefore, recommends that unless this sector has developed large surpluses to the extent of enabling the country to undertake regular exports, it would not be advisable to permit futures trading in foodgrains.

(4.6)

(ii) **Cotton and Kapas**

(a) **Cotton**

The supply position of cotton has considerably improved in recent years as compared to the position in 1966 when futures trading was prohibited. There have been no imports during the last two years. Exports of selected varieties have been permitted. Although consumption of cotton by mills has been increasing, large stocks of it have to be carried forward by the functionaries in the trade. Despite the operations of the CCI, the MSCMF and the co-operative sector over a number of years, the cotton economy has remaind a market oriented economy, as more than 50 per cent of the cotton is still marketed by the cotton trade and fluctuations in the prices of different varieties have remained quite large. The MSCMF needed the facility of futures trading in cotton in view of the large stocks it had to handle exposing it to the risk involved in price fluctuations. The Committee, therefore, recommends that futures trading may be resumed in cotton at a few well selected centres.

(4.16, 4.17 and 4.18)

(b) **Kapas**

The marketing of kapas is seasonal, as in that form it remain in the market only for about three to four months. Moreover, tradition of futures trading in kapas is only in certain parts like Punjab and Saurashtra. The Committee, therefore, recommends that futures trading may be permitted in kapas at a few centres where there has been long tradition of such trading and where functioning of competitive futures markets is possible.

(4.19)

(iii) Raw Jute and Jute Goods

(a) Raw Jute

The supply of raw jute (including mesta) is large and sizeable stocks have generally to be carried forward from season to season. The demand for jute is exclusively from jute mills and it is reckoned around 75 lakh bales annually. Exports have been negligibe so far but may have to be allowed in larger quantities to support prices in view of the increased surplus. The statutory minimum prices and the operations of the JCI have not brought adequate relief to the farmers and, often transactions are reported to be taking place at less than the statutory minimum prices. This indicates the need for supporting the existing mechanisms. Taking into account the supply and demand position in raw jute and the existing marketing arrangements the Committee is of the view that futures trading in raw jute can play a useful role to bring benefits to growers, stockists and other functionaries in the trade. The facilities of tsd and ntsd contracts serve the purpose of entering into long-term commitments and carrying adequate stocks safely if such facilities are coupled with futures trading facilities also. The Committee, therefore, recommends that futures trading in raw jute should be permitted.

(4.21 and 4.25)

(b) Jute Goods

Sacking

The main items of production in jute goods are hessian and sacking and there has been tradition and demand for futures trading only in these items. The facility of futures trading in sacking has been made use of by the dealers, who sell to the domestic consumers, and the shippers who sell to the overseas buyers. The hedge market in sacking is also used for hedging stocks and PDOs. The sacking futures market has functioned satisfactorily. The Committee, therefore, recommends its continuance.

(4.30)

Hessian

The bulk of the production of hessian is exported. Immediately after the conclusion of a export deal, it is not possible for the exporters to get the required goods through tsd contract, since the construction of quantum required may not be readily available. This makes it necessary for the exporters to cover their export commitments in a futures market simultaneously with the export sale. The absence of futures trading facilities results in loss of export business and in some cases export markets. Hedging facilities would increase the competitive capacity of the exporters against other jute goods producing countries and synthetic substitutes. Further, the competitive prices quoted in the futures market help to reduce monopolistic tendencies in the internal market. The Committee, therefore, recommends that futures trading in hessian should be permitted.

(4.31)

Carpet Backing

Carpet backing is produced by the mills as per the specifications of the foreign buyers and supplied to them directly. There is no domestic market in it and there has not been any demand for futures trading. The Committee, therefore, does not consider it necessary to permit futures trading in carpet backing for the present.

(4.32)

(iv) Edible Oilseeds and Oils

Although the total production of major edible oilseeds and oils is large in absolute terms, a serious secular shortage of these commodities in relation to the demand has emerged in this country. This has resulted in large, violent and frequent fluctuations in proces of major oilseeds oils. Under these circumstances, in our opinion, edible oilseeds and oils are not, in the present stage, commodities fit for being permitted for futures trading as it is not clear whether social gains through futures trading will be larger than private gains. The Committee, therefore, recommends that futures trading in edible oilseeds and oils should not be permitted for the present. The Committee would like to point out that it is extremely important to augment the supplies and to reduce the fluctuations in availability and indeed to restrain demand to the extent possible. As the primary cause of restricted supplies in relation to high demand is the absence of any major break-through in the production technology of these commodities, it is to be recommended that large resources, e.g. research and development, should be devoted to edible oilseeds. Until this happens, the Committee further suggests that the regulatory mechanism already in operation should be continued and further strengthened. Only when supply is augmented, an important condition for the operation of futures market might emerge in these commodities in future.

(4.37, 4.38 and 4.39)

(v) Castorseed

A study of the price behaviour indicates that there is no direct relationship between the prices of castorseed/castor oil and those of groundnut oil and that the ban on futures trading in castorseed had not helped in exercising a stabilising influence on the prices of groundnut oil. This is mainly because the total annual production of castor oil, a non-edible commodity as distinct from groundnut oil, forms only an insignificant proportion of the total production of groundnut oil. Being export oriented with about 50 per cent of castor oil produced finding an outlet to the overseas markets, the prices of both castorseed and castor oil are determined to a great extent by the developments taking place in the international markets. Taking into consideration this important aspect as also the pleadings made by the various concerned interests including STC, the Committee recommends that futures trading in castorseed should be resumed.

(4.44 and 4.46)

Castor Oil

The facility of futures trading has been sought by all the concerned interests only in castorseed and not in castor oil. Besides, the market for castor oil is quite narrow and futures trading in this country has been conducted only in castorseed. Further, the need for hedging in castor oil can be met through the facility of futures trading in castorseed. The Committee, therefore, recommends that there is no need for futures trading in castor oil.

(4.47)

(vi) **Linseed**

The rise in the production of linseed, emergence of sizeable carry-over stocks in recent years, and the absence of any direct relationship between the prices of linseed oil and edible oils are points in support of futures trading in linseed. Further, since as much as about two-thirds of the production of linseed oil is used for non-edible purposes, viz., industrial use, the argument that futures trading in linseed should not be permitted because linseed oil is used for edible purposes does not carry sufficient conviction. Futures trading in linseed had been permitted uninterruptedly for about 20 years till it was banned in February 1977. Futures trading in this commodity had functioned satisfactorily. We, therefore, recommend that futures trading should be permitted in linseed.

(4.53)

Linseed Oil

Exports of linseed oil are at present banned and there has neither been any tradition of futures trading in linseed oil nor any demand for such trading from the concerned interests. Moreover, the market for linseed oil is quite narrow. Hence, we do not consider it necessary to permit futures trading in linseed oil.

(4.54)

(vii) **Oilcakes**

Oilcakes may be broadly grouped into major and minor oilcakes. In the case of minor oilcakes like mahua oilcake, neem oilcakes etc., not only their production is quite small, but also there is no assured supply of even a minimum quantity. In view of this and the extremely small size and unorganised nature of the markets in minor oilseeds, the Committee considers that there is no case for permitting futures trading in any of the minor oilcakes at present.

(4.60)

As regards major oilcakes like groundnut, cottonseed or rapeseed oilcakes, the Committee has looked at the whole question primarily from the point of view of promoting exports of extractions. The expeller oilcake contains six to seven per cent oil and it is in the interest of not only the domestic consumers of edible oils but also of the extraction industry that this oil is extracted within the country itself. The Government of India have already banned the exports of all expeller oilcakes. Further, futures trading in groundnut expeller cakes, which in terms of production accounts for the bulk of the total production of expeller oilcakes, was banned due to rising prices of the groundnut group of commodities. In respect of other expeller oilcakes like rapeseed cake, linseed cake, such trading was banned because of their misuse for trading in banned commodities. In view of the position as aforesaid, we consider that there is no need for permitting futures trading in expeller oilcakes for the present. As regards extractions, the supply is quite large, the demand for it, which is mainly from overseas buyers, is uncertain and the international market for it is highly competitive. The quantum of exports of extraction is sizeable. The commodity is also suitable for futures trading. Properly organised futures markets in major extraction cakes would be useful for promoting their exports. Since, on the basis of production and exports, groundnut extractions have been found to be eminently suitable for being traded on a futures market, the Committee recommends that initially this facility may be extended in respect of groundnut extractions and extended to other major extractions such as rice branoiled cake. However, the actual opening of futures markets should follow the coming into existence of a representative association at a suitable centre.

(4.62 and 4.63)

(viii) **Pepper**

The supply of pepper during a season is fairly large. Out of an annual production of about 35,000 tonnes, the domestic consumption forms only about one-third and the rest is available for export. The overseas demand for the commodity is susceptible to wide variation causing undue price fluctuations which results in hardships to the producers, stockists and exporters. The facility of futures trading in pepper is extensively used by exporters and stockists. Taking into account all these factors, the Committee recommends that futures trading in pepper should be continued.

(4.67)

(ix) **Turmeric**

Due to large variability in supply and inelastic demand, turmeric prices are susceptible to wide fluctuations. This would necessitate hedging facilities for those who carry large stocks of the commodity in the process of marketing. Futures prices by serving as advance indicators have exercised, during periods of sharp fall or rise in the ready prices, a restraining influence on them. The dealers and exporters benefitted from the futures market in turmeric, the former by hedging their stocks and the latter by purchasing on the futures market against their actual export commitments. The experience of regulation of futures trading in turmeric has been satisfactory. The Committee, therefore, recommends that the facility of futures trading in turmeric should be continued.

(4.70 and 4.71)

(x) **Sugar and Gur**

(a) **Sugar**

In view of large variations in the supply of sugar and the demand for it continuously rising, sugar has been subjected to control of one form or the other. Taking into account the special circumstances in which the market in sugar functions, the Committee recommends that there is no need for futures trading in it. If, however, the present pattern of marketing of sugar is to give place to a system of free market, then the case for futures trading could emerge as a mechanism which would provide the advantages of such trading to the various functionaries in the trade. It would also then be of benefit to the producers and consumers.

(4.73 and 4.74)

(b) **Gur**

Gur has neither been subjected to any fixed price nor to any other form of control at any point of time, while a major portion of sugar coming under the levy scheme has remained controlled at various points from time to time. Hence, in periods of shortages when the demand for sugar exceeds its supply, the price of levy sugar does not change but the excess demand is transferred to the gur market, which is free, leading to a sharp rise in the prices of gur. Conversely, in times of surplus, the controlled sugar prices do not register much of a downward move, but the full impact is transferred to the gur market leading often to an undue fall in the prices of gur. Such wide fluctuations in gur prices seem to make a strong case for futures trading in gur. However, the factors in respect of gur which required special consideration are that despite the tradition of futures trading, there are no well-defined and acceptable standards in respect of gur and hence the grades as understood in different markets do not have close relationship with one another. Further, gur cannot be stored for long without deterioration in its quality. In view of these factors, we consider that while there is an inherent need for futures trading facilities in gur, such trading would require much closer supervision both by the recognised associations and the Forward Markets Commission. We recommend that futures trading in gur should be permitted as a policy on a continuous basis save in exceptional circumstances brought about by acute shortage of sugarcane, when the Government or the Forward Markets Commission might, if the situation so warrants, suspend it for the time being. Such suspension, however, should be temporary and futures trading should be restored as soon as possible. At the same time, when futures trading is permitted in the commodity, it should not be for any specified period since that leads to uncertainty and speculation having unhealthy effect on the working of futures markets. Further, the associations recognised for gur should be such as to be able to deal with the special problems of the commodity, particularly those relating to standardisation and grading, and should have qualified personnel and resources to deal with such problems.

(4.76, 4.77 and 4.78)

(xi) **Silver**

India's production of silver is negligible and its supply is limited. Silver has become a very important industrial material and has also acquired strategic importance. As a result, the stocks of silver are getting depleted over the years. Exports of silver are not permitted. Silver market has also become volatile, of late, with very abnormal variations in prices and these abnormal conditions are expected to continue in the foreseeable futures. Taking all these factors into consideration, the Committee is of the view that there is no case for permitting futures trading in silver at present.

(4.82)

(xii) **Other Commodities**

Futures trading in India has, so far, been confined to certain commodities in which there has been a long tradition of such trading. However, it was represented to us that there has been a substantial increase in the production of many other commodities in excess of internal demand, necessitating their exports in large quantities and if futures trading in those commodities could be organised, it would serve as an advance indicator of the future trend of prices to producers who would then plan their production and offer hedging facilities to other functionaries. The commodities indicated in this regard were cardamom, coffee, tobacco, tea, ginger, chillies, onion, potatoes, apples, etc. While the Committee could not study all these commodities for lack of time, the position in regard to some of them, which could be studied in some detail, are as follows.

(4.83)

(a) **Cardamom**

Although production of cardamom is not very large in absolute terms, in value terms the commodity assumes importance. From the export angle, the commodity is significant since the bulk of the production is exported and the foreign exchange earnings from it are quite sizeable. However, there are no adequate cold storage facilities under which condition alone the quality of it can be fully preserved. As a result, stocks are not carried forward on any large scale beyond a period of three months or so. We are of the opinion that these difficulties are not insurmountable and with the building up of the necessary infrastructure this commodity would become suitable for futures trading. We, therefore, recommend that the Commission should keep this commodity under watch and advise the Government regarding introduction of futures trading in it at appropriate time. Once this happens, further developments in the marketing structure may get accelerated.

(4.85)

(b) **Coffee**

Coffee is, no doubt, suitable for futures trading as it has standardised grades. However, the functioning of a board futures market, within the present institutional arrangements for marketing in our country, is not possible since the releases of coffee are controlled and no body except the registered traders is permitted to purchase coffee. The question of introducing futures trading in coffee can be considered only when free trading in coffee is introduced.

(4.87)

(c) **Tobacco**

The supply of tobacco is large and there have been wide fluctuations therein. Further, the demand is uncertain since a part of it comes from overseas buyers. Fluctuations in the prices of the commodity are quite large and the growers generally do not get remunerative prices. Though the present system of gradation is not fully satisfactory, the commodity is amenable to a proper system of gradation. However, the present market structure in tobacco is imperfect in the sense that the manufacturer-buyers are limited in number and they are in a position to dictate the terms to the sellers. There are no organised markets for ready and forward transactions. In the above context, the Committee is of the view that the commodity being suitable for futures trading, it would be advisable for the Tobacco Board and the concerned interests to take early steps to provide a proper system of ready and futures market in the commodity.

(4.90)

(d) **Tea**

The production of tea in the country is large and a substantial quantum is exported. There are also gluts and shortages in this commodity leading to large variations in its prices. The commodity being export oriented, the facility of futures trading would be to the advantage of the exporters and will contribute to export promotion. Although there are innumerable qualities of tea, it should be possible to evolve a suitable futures contract. However, the necessary institutional framework would have to emerge before the actual opening of futures trading. The Committee, therefore, recommends that the Tea Board and the concerned interests should work towards the evolution of such a framework so that futures trading in tea is possible.

(4.92)

As regards commodities like potatoes, onions, apples, ginger, chillies, etc., the supply position in them has been comfortable in recent years owing to significant increases in their production. In fact, in some of them like potatoes, onions and apples, there have been gluts leading to uneconomic prices to the growers and subsequent short-fall in production leading to high levels of prices for the consumers. The existence of futures markets will enable the stockists and dealers to act as a cushion in periods of excess production and shortages since they would be able to cover their own risks in the futures markets. The introduction of futures trading may itself help to some extent the process of building up the necessary infrastructure required for efficient marketing. The Committee, therefore, recommends that these commodities too should be kept under watch by the Commission so as to take timely steps for introducing futures trading in them.

(4.93)

Basic requisites for the regulation of futures trading

10. The maintenance of competitive character of a futures market should be the most important consideration in the regulation of futures trading. The location of centres for establishing future markets, selection of suitable associations for conducting trading at the centres, rules and regulations subject to which such trading should be permitted, regulatory measures that may be introduced by the Commission to contain excessive speculation, etc., need to be considered from this point of view.

(5.2)

(a) As regards choice of a centre for the location of a futures market, we recommend that, as far as possible, the number of recognised futures markets in any commodity should be limited to the minimum necessary to avoid dispersal of hedge and speculative business over a number of markets making them in the process thin and less competitive. This would also facilitate more effective regulation of the recognised markets by the authorities concerned.

(5.6)

(b) The present provision in section 15(4) of the FC(R) Act of permitting members to appropriate the business of non-member clients, although with their consent, is not conducive to maintaining the competitive character of futures trading. We, therefore, recommend that the present provision of permitting members to appropriate non-member's business outside the trading ring should be deleted and the FC(R) Act as well as rules and regulations of the recognised associations should provide that all business of non-members shall be put through in the ring by an outcry and any member of the association should have an opportunity to enter into an opposite transaction with the non-member at the most competitive rate offered in the ring.

(5.7)

(c) We feel that since the futures markets are primarily established to offer hedging facilities, the Commission's measures should not be such as to impair the utility of these markets for the purpose of hedging. We are of the view that while reasonable restrictions on speculative open positions as opposed to hedge open positions and reasonable limits on periodical fluctuations in prices are in conformity with the basic purpose for which futures markets are established, very stiff special margins linked with the futures price

levels and maximum and minimum prices only in respect of futures contracts should be examined critically and in any case used sparingly.

(5.9)

11. At present the Commission requires the members of recognised associations to submit returns normally on weekly basis and, in special circumstances, on daily basis. The present system of reporting is defective in many ways. First, it does not bring out the most vital information regarding the extent of hedging for which the markets are established. This information can be obtained by requiring each operator to disclose the break-up of his open position as hedge position and speculative position separately under a statutory requirement. Secondly, the present practice of requiring members to indicate the trading details of their non-member clients is not likely to bring forth correct information. We, therefore, recommend that periodical return on the lines indicated in the proforma given in Annexure XIII may be prescribed by the Commission and all operators—members as well as their non-member clients—should be required to submit it to the Commission.

(5.10)

12. We recommend that in a commodity in which more than one futures markets have been established initially, even when such markets are few, their continuance should be periodically reviewed on the basis of the extent to which the established markets have been used for the purpose of hedging.

(5.11)

13. Since many of the manipulative tendencies in the futures market arise through trading in the name of non-members, it is desirable to have a more direct control on the activities of non-members than at present. This can be achieved by requiring all non-members desirous of trading in a futures market, to register with the Commission through the concerned recognised association subject to such rules and conditions as may be prescribed by the Commission for the purpose. We also recommend that the recognised associations should be required to lay down in their rules, certain minimum margin or deposit, ranging between say 5 to 25 per cent of the value of the contract, to be obtained by a member from each non-member. In order to protect the non-members in respect of such margin or deposit, it should be laid down in the FC(R) Act that the amounts collected by the member should be held in segregation by the member concerned and not commingled with his own funds.

(5.13, 5.14 and 5.15)

14. On many occasions, running hedge contracts under the auspices of the recognised associations are suddenly closed out by the members acting in concert or by the Boards of recognised associations before the actual due date of the contract, at rates arbitrarily decided upon. The Committee recommends that the rules and regulations of the recognised associations should make special provisions to prevent these types of malpractices and such activities on the part of any association should be considered serious enough to justify the withdrawal of recognition of such an association.

(5.16)

15. Having recommended continuation or immediate resumption of futures trading only in such commodities in which it is economically and socially desirable and also introduction of a proper scheme of regulation, we recommend that the Government should adopt a long-term policy in respect of futures trading. Once it is permitted, it should be continued without any interruption except in very abnormal situations when it might be necessary to suspend it in a particular commodity for a short period.

(5.17)

16. We suggest that it should be the endeavour of the Government and the Forward Markets Commission to develop the associations recognised for futures trading in the country into modern commodity exchanges. We hope that the existing associations will take heed of these suggestions and strive towards such institution building.

(5.18)

Non-transferable specific delivery contracts

17. The need for the facility of ntsd contracts to various trade interests arises mainly for ensuring in advance a smooth and assured supply of and demand for the commodity in the future period. A large proportion of buying and selling in the commodity markets is through the medium of ntsd contracts of duration of two to five months though contracts of much longer duration, particularly in manfactured commodities like cloth or steel or tools, are also often entered into.

(6.4 and 6.6)

18. The experience of the Forward Markets Commission showed that ntsd contracts were used for camouflaging futures trading in banned or regulated commodities. In a large number of commodities ntsd contracts were either prohibited by applying section 17 of the FC(R) Act or were not permitted to be traded in the commodities to which section 15 of the Act had been applied. We have come to the conclusion that permanent ban or prolonged suspension of ntsd contracts is no solution. The prolonged prohibition of ntsd contracts is causing genuine hardships to important functionaries in different commodities. We have already recommended in Chapter 7 that the present scheme of the FC(R) Act enabling the Government to regulate ntsd contracts, when necessary, should be retained. We consider that, along with other amendments suggested by us, this is an adequate safeguard to control any possible use of ntsd contracts for speculative purposes. The Commission's experience of regulating ntsd contracts has been very satisfactory. Taking all these factors into account, we recommend that the prohibition imposed on ntsd contracts in important commodities (like major edible oilseeds such as groundnut, mustardseed

and cottonseed and their oils, coconut oil and foodgrains, which are no more subjected to zonal restrictions) should be lifted and such contracts in them should be permitted under the auspices of properly selected recognised associations representing different functionaries dealing with the actual commodity.

(6.8 to 6.11)

19. The principles followed by the Commission in selecting associations for recognition in respect of ntsd contracts have been stated in the Commission's Report on the Recognition of Association in respect of ntsd contracts in Indian Cotton submitted to the Government in April 1972. We are generally in agreement with these principles and would, therefore, recommend that the Commission should proceed on the basis of these principles for regulating ntsd contracts in important commodities in which such contracts cannot be permitted freely. The need for continuing regulation of these contracts in the commodities in which they are regulated should be examined by the Forward Markets Commission at regular interval and necessary recommendations made to the Government.

(6.12)

20. In the case of commodities other than the major commodities mentioned above, we recommend that trading in ntsd contracts may be permitted freely after the amendments proposed in this report to the definition of ntsd contract and other related matters have been carried out. The Forward Markets Commission should keep a watch on the working of such contracts through its Enforcement Directorate. If the facility for free trading in ntsd contracts in any of these commodities is found to be misused by unscrupulous elements for speculative purpose, the question of bringing them under regulation should be considered by the Commission as and when necessary.

(6.13)

Amendments to FC(R) Act

21. There is no need to change the present scheme of classification of contracts or regulation as the experience relating to the enforcement of the FC(R) Act has clearly indicated that the present approach is broadly correct. To ensure that ntsd contracts are not used for (i) camouflaging speculative trading to evade ban or restrictions imposed by the Government on futures trading in the commodities, or (ii) acquiring pre-emptive hold on large future supplies of the goods concerned, it is necessary to provide for their regulation, whenever necessary as at present. There is however, a strong case to amend the definition of ntsd contract to make it precise and to provide for certain facilities required by genuine trade.

(7.12)

22. We feel that in order to make the Act effective, it is necessary to prevent illegal forward trading in regulated or banned commodities conducted in the guise of unregulated or unbanned commodities. We therefore, recommend that the Act should be amended to provide that (i) all trading in transferable contracts (i.e. forward contracts other than ntsd contracts), which is not regulated or controlled by an association, shall be illegal, and (ii) no association regulating and controlling transferable contracts shall do so without obtaining a certificate of recognition from the Government except when the Central Government has specifically exempted any commodity from this requirement of recognition. The net effect of these two provisions in the Act would be that trading in all transferable contracts (and in ntsd contracts when such trading is specifically regulated) will be under the auspices of recognised associations only and there will be no need for a separate category of registered associations. The possibility of conducting illegal futures trading in the name of so-called party to party contracts would thus be eliminated. In our view, these restrictions cannot be construed as unreasonable for reasons mentioned in paragraph 19 of Chapter 7.

(7.17 to 7.22)

23. The Commission had suggested to the Government a number of amendments to the Act in October 1978 (Annexure XV). These amendments were referred to this Committee for its views. We agree with the amendments suggested by the Commission such as (i) to definitions of ready and ntsd contracts, (ii) to tighten the penal provisions by increasing the maximum and minimum fines and imprisonment, to provide for compulsory imprisonment for the first offence and to remove discretion to the Magistrate to release the offenders under the FC(R) Act by taking recourse to provisions of the Probation of Offenders Act and (iii) to make presumption under section 22B applicable to seizures effected both with or without a warrant, and others except those for powers for search and seizure. This is because none of the Commission's Officers except the Director of Enforcement, is equipped by training and temperament to exercise such powers and if such powers are vested in the Commission, the police authorities may no longer consider themselves solely responsible for investigation for offences under the FC(R) Act and their full co-operation may not be easily forthcoming.

(7.25 to 7.33 and 7.37 to 7.43)

24. The amendments suggested by the Commission to the definitions of the terms association, registered association and in respect of other matters relating to registered associations will not be necessary if the amendments suggested by us in paragraph 22 above are accepted as in that case, the category of registered associations would stand abolished. The amendments suggested by the Commission would, however, be necessary in case our suggestions are not accepted.

(7.34 to 7.36)

25. The Commission had made a proposal for adjudication of offences under the Act by the Commission. We recommend that instead of providing for adjudication of offences by the Commission, the offences under the Act should be made compoundable with the sanction of the Commission. This would enable the Commission to get quick disposal of a large number of cases pending for long in law courts without the need

for setting up a cumbersome and costly adjudication machinery which will have to remain idle for most of the time.

(7.44 to 7.46)

26. We have also recommended amendments for (i) registration of all non-members trading in futures markets, (ii) submission of periodical returns by all operators, members as well as non-members directly to the Commission showing the volume of trading and break-up of the open position as hedge and speculative positions, (iii) requiring all business of non-members to be put through trading ring of recognised associations by public out-cry, and (iv) requiring each member of the recognised association to obtain from his non-member client a minimum margin or deposit which should be held in segregation without commingling with his own personal funds.

(7.47)

Strengthening of the Forward Markets Commission

27. If the recommendations of the Committee in respect of various matters are accepted by the Government, it would substantially enlarge the role of the Commission. The Committee notes that two posts of Member out of four provided under the FC(R) Act have remained unfilled for long. It is necessary that the vacant posts be filled so that a better division of labour regionally, functionally and commodity-wise and better handling of the volume of work can be brought about. As the Commission has to deal with persons and agencies of the highest standing in the trade, commerce and manufacture, it is important that the official standing of its Members and Chairman should be of a high level. It is, therefore, recommended that the Chairman of the Commission be given the status of an Additional Secretary and the Members of a Joint Secretary in the Central Government.

(8.1 and 8.2)

28. The staff strength of both the Commodity and the Enforcement Divisions of the Commission will have to be appropriately strengthened in the light of our various recommendations to enable the Commission to discharge its functions more comprehensively and efficiently. Having regard to the selective approach to futures trading which we have recommended, the magnitude of illegal forward trading in the country and the potential for anti-social elements devising ingenious methods to conceal such trading, we feel that the present enforcement arrangements in the office of the Commission are totally inadequate to cope with the task of combating illegal forward trading. The major pockets of illegal forward trading are located in the States of Gujarat, Rajasthan, Punjab, Haryana, Uttar Pradesh, Madhya Pradesh and the Union Territory of Delhi and the Cities of Bombay and Calcutta. Taking into account the above factors, we recommend that Regional Offices of the Commission may be established, in addition to the one already at Calcutta, at Delhi, Ahmedabad and Lucknow to begin with. These offices should be under the charge of a gazetted officer who should be assisted by supporting staff at the level of senior/junior research assistants and necessary subordinate staff. The establishment of such small Regional Offices would be feasible economically and assist in the efficient discharge of the responsibilities of the Commission under the FC(R) Act.

(8.4 to 8.7)

29. There is no regular research unit manned with staff having adequate statistical and econometric qualifications in the office of the Commission to undertake specialised studies. The Commission should undertake research activities to cover various aspects of futures trading since the potential for such research studies is quite wide.

(8.8)

30. The timely publication of the data regarding recognised futures markets in the Forward Markets Bulletin brought out by the Commission would be of much help to the Government in framing its policies and also to the trading community in adopting a responsible approach towards futures trading.

(8.9)

(A. M. Khusro)
Chairman

(L. S. Venkataramanan)
Member

(B. N. Kapre)
Member

(Vijay L. Kelkar)
Member

(P. N. Kaul)
Member

(V. N. Lokur)
Member

(M. G. Jawle)
Member-Secretary

NEW DELHI :
30*th June,* 1980

ANNEXURE I

GOVERNMENT OF INDIA ORDER CONSTITUTING COMMITTEE ON FORWARD MARKETS

GOVERNMENT OF INDIA

MINISTRY OF COMMERCE, CIVIL SUPPLIES & CO-OPERATION
(DEPARTMENT OF CIVIL SUPPLIES & CO-OPERATION)

ORDER

No. 10(3)-IT/77. *New Delhi, dated the March* 27, 1979

SUBJECT: **Constitution of a Committee to Review the operations of Forward Markets and the Role of the Forward Markets Commission.**

The Government of India have decided to set up a Committee to look into the operations of forward markets and the role of the Forward Markets Commission to effectively regulate the futures trading and futures markets in various commodities with a view to curb unhealthy trends, and also to implement the Government's decision prohibiting forward trading in specified commodities. The composition of the Committee will be as follows :

Dr. A. M. Khusro, ... Chairman
Vice-Chancellor,
Aligarh Muslim University,
Aligarh.

Shri L. S. Venkataramanan, ... Member
Head,
Agricultural Development and Rural Transformation Unit,
Institute for Social & Economic Change,
Bangalore-40.

Shri B. N. Kapre .. .. Member
Chairman,
Forward Markets Commission,
Bombay.

Dr. Vijay L. Kelkar, ... Member
Economic Adviser,
Deptt. of Commerce.

Dr. P. N. Kaul, ... Member
Additional Economic Adviser,
Deptt. of Civil Supplies & Coopn.

Shri M. G. Jawle, ... Member-Secretary
Member,
Forward Markets Commission,
Bombay.

The Committee may co-opt such other Members as may be considered necessary.*

2. The terms of reference of the Committee will be as follows :—

(i) To review the role that forward trading has played during the last 10 years ;

*Shri V. N. Lokur, Joint Secretary to the Government of India, Ministry of Law, Justice & Company Affairs, (Deptt. of Legal Affairs), Bombay, was co-opted by the Committee at its meeting held on the 23rd April, 1979.

(ii) To assess the role that forward trading can play in the prevailing economic conditions and marketing/distribution system in the commodities in which forward trading is possible, particularly in commodities in which resumption of forward trading is generally demanded;

(iii) To examine the extent to which forward trading in commodities in which such trading may be permitted could be of direct or indirect benefit to producers and consumers of the commodities;

(iv) To examine the extent to which forward trading has special role to play in promoting exports ;

(v) To suggest measures to ensure that forward trading in the commodities in which it is allowed to be operative remains constructive and helps in maintaining prices within reasonable limits ;

(vi) To suggest amendments to the Forward Contracts (Regulation) Act in the light of its recommendations particularly with a view to efficient enforcement of the Act to check illegal forward trading when such trading is prohibited under the Act; and

(vii) To suggest measures for strengthening the Forward Markets Commission to achieve the objective of making futures trading socially purposeful.

3 The Committee may meet at New Delhi or such other places in the country as it considers necessary. The Forward Markets Commission, Bombay, will provide requisite secretarial assistance to the Committee and also meet the T.A. and D.A. of the Chairman and non-official members of the Committee in respect of journeys undertaken by them in connection with the work of the Committee.

4 The Committee will submit its report to the Government within a period of six months@.

Sd/-

(A. S. Sethi)
Joint Secretary to the Govt. of India

Copy to :

1. Chairman and all Members of the Committee.
2. Secretary, Forward Markets Commission.
3. Secretary, Department of Commerce, New Delhi.
4. Secretary, Department of Agriculture, New Delhi.
5. Secretary, Department of Economic Affairs, New Delhi.

ANNEXURE II

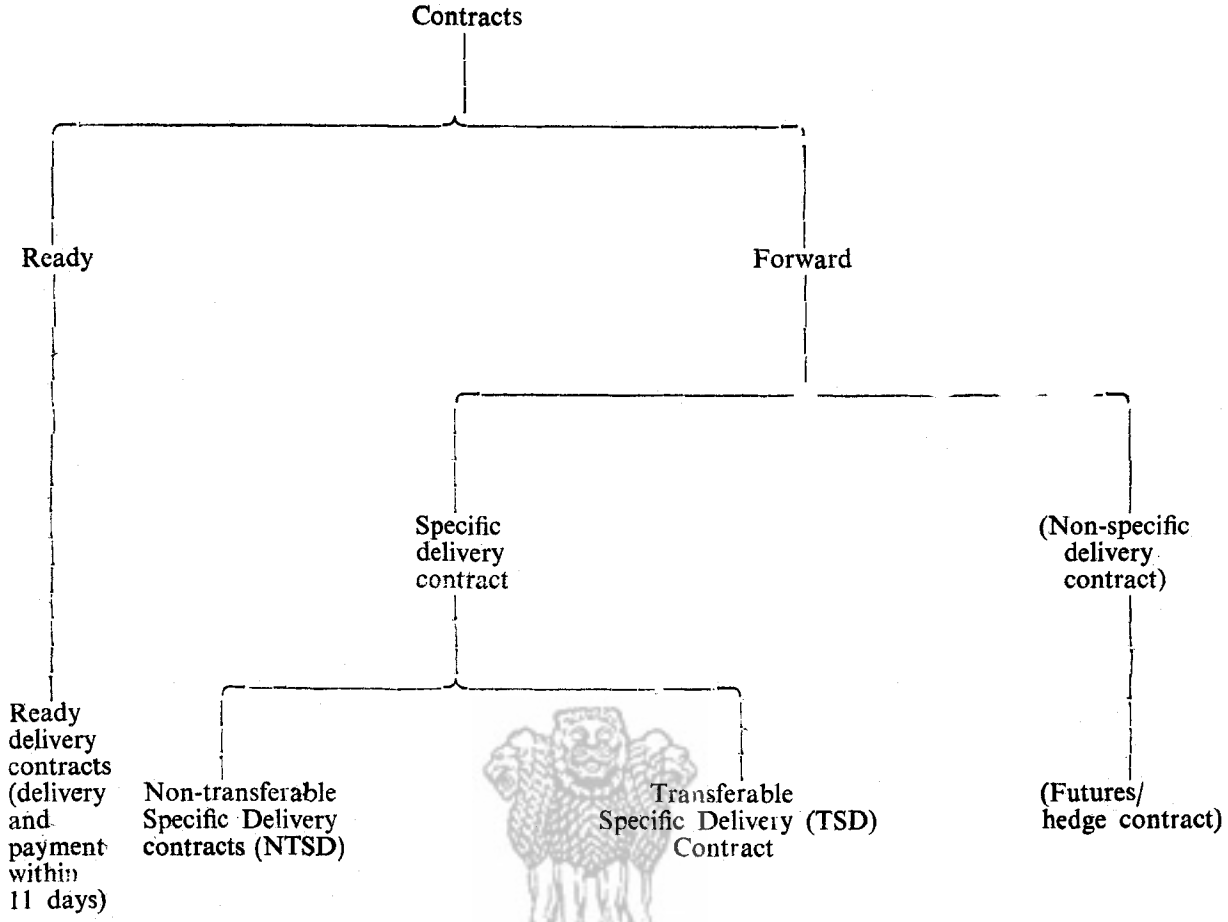
QUESTIONNAIRE ISSUED BY THE COMMITTEE

A. Introductory note to the Questionnaire

The Forward Contracts (Regulation) Act, 1952 was passed by the Indian Parliament in December 1952 to provide a central legislation in respect of forward trading, which was included in the Union list of powers under the Indian Constitution adopted after independence. The FC(R) Act, 1952 is an enabling measure and its regulatory provisions are applied by notification to particular commodities and areas. It prohibits options and provides for the regulation of what are known as "non-transferable specific delivery contracts" and "transferable specific delivery contracts" including "futures" or "hedge contracts". The regulation of Forward trading in a commodity, when the regulatory provisions of section 15 of the Act have been applied to the commodity, is to take place through the associations recognised for the purpose under the Act, but such recognised associations have to work under the general supervision and direction of a special statutory authority established under the Act, viz., the Forward Markets Commission.

@The time limit for submission of the Report of the Committee was extended by the Government upto the 30th June, 1980 vide Orders No. 14(1)-IT/79 dated the 5th November, 1979 and No. 14(1)-IT/79 dated the 2nd April, 1980.

2. The scheme of the classification of different types of contracts implied under the FC(R) Act. 1952 is as follows:—



However, in the FC(R) Act, only ready delivery contracts and specific delivery contracts viz., NTSD contracts & TSD contracts have been defined. The terms 'non-specific delivery contract' and 'futures contract' used in the above table have not been used. The "futures/hedge" contract has been left undefined and only by implication treated as a non-specific delivery contract to be regulated under the FC(R) Act, 1952.

3.1 The distinction made by the Act between non-transferable specific delivery contracts on the one hand and transferable specific delivery contracts or hedge or futures contracts on the other rests principally on the conditions relating to the delivery of goods against the contracts and the mode of their settlement.

3.2 In non-transferable specific delivery contracts delivery of goods is a common feature. The goods have to be of a specified quality and have to be delivered in a specified quantity at a specified destination for a specified price at a specified date and to a specified party. This type of contract resembles the ready contract except that the delivery of goods takes place after a period of eleven days. Under a transferable specific delivery contract, delivery takes place between the first seller and the last buyer since the contract is transferable from hand to hand, but it has to conform to the same detailed specifications as the non-transferable contract. Hedge or futures contracts, however, do not visualise actual delivery at all, except in a residual sense as they are entered into not for giving or taking delivery but either for hedging or for speculative purposes.

3.3 The settlement in a non-transferable specific delivery contract takes place through the payment of the full value of goods by the buyer to the seller. The hedge or futures contracts and transferable specific delivery contracts in so far as the intermediate buyers and sellers are concerned are, however, settled by the payment of differences between the prices at which the contracts were bought and the prices at which they were sold.

3.4 The transferable specific delivery contract thus occupies a position intermediate between the non-transferable specific delivery contract on the one hand and the futures or hedge contract on the other. It has points of resemblance to both.

Items in which forward trading is prohibited and regulated at present

4. Since the enactment of the FC (R) Act in 1952, the regulatory provisions of the Act were applied from time to time to a number of commodities with a view to permit forward trading in such commodities only under regulation. By 1963, regulated futures markets were established under the auspices of 30 recognised associations in 15 commodities

which included all the principal commodities in which there was a tradition of future trading such as cotton, kapas, oilseeds like groundnut, mustardseed, cottonseed, castorseed and linseed, groundnut oil, silver, gur, jute and jute goods, pepper, turmeric etc. With the emergence of shortages in the economy, futures trading in most of these commodities came to be progressively banned or suspended. At present futures trading is permitted at recognised associations only in 4 commodities, viz., jute goods (sacking), pepper, turmeric and gur. Trading in tsd contracts is permitted under the auspices of the recognised association in raw jute and jute goods. Trading in ntsd contracts in most of the commodities like oilseeds, oils etc., came to be banned or suspended as the name of these contracts was invoked by speculators for camouflaging their speculative trading in the banned commodities. In certain important commodies like cotton, groundnut and groundnut oil, raw jute and jute goods, ntsd trading was regulated under the auspices of recognised associations which were required to frame detailed bye-laws for the purpose. However, with the emergence of acute shortage and State restrictions (formal or informal) on the movement of groundnut and groundnut oil, ntsd contracts in these came to be suspended. At present, trading in ntsd contracts is permitted under the auspices of recognised associations only in cotton, raw jute and jute goods.

B. Questionnaire

Organisation

1. Please furnish the following information.

(i) Name and Address of the Association.

(ii) Membership indicating panelwise classification and strength in each panel.

(iii) Commodities for which your Association is recognised/registered under the FC(R) Act, 1952 and the type of forward contract (i.e. futures contract/transferable specific delivery contract/non-transferable specific delivery contract) regulated by your Association.

(iv) How long your Association has been concerned with forward trading and the names of commodities in which you have so far conducted forward trading and those in which you are at present conducting such trading.

(v) Please furnish the following data commoditywise for the last 5 years :

(a) Production of the commodities for the region commanded by your Association indicating the districts covered.

(b) Monthly volume of forward trading by types of contracts.

(c) Highest, lowest and month-end open position.

(d) Monthly average prices of ready, futures and tsd contracts.

(e) Monthly highest and lowest ready and futures prices.

2. Do you consider the present classification of contracts under the FC(R) Act into ready and forward contracts and further classification of forward contracts into non-transferable specific delivery contracts, transferable specific delivery contracts (including hedge contracts) as economically justifiable. Have you any suggestions in this regard from the point of view of utilisation of different types of contracts for undertaking efficient marketing of the commodities ?

3. (a) In which of the commodities, with which you are concerned, would you consider that forward trading should be permitted ?

(b) Please clearly indicate which type of forward contracts need to be permitted.

(c) Give full justification for the need of different types of contracts for each of the commodities concerned, taking into account the present and expected supply and demand situation, needs of different functionaries involved in the marketing of the commodity, effects of such trading on prices and on producers, intermediaries, processors, importers, exporters, final consumers, etc.

4. Do you think that futures or hedge trading can play a useful role in the prevailing economic conditions and marketing and distribution arrangements in force in various commodities with which you are concerned? Please give detailed comments with justification in support of your contention taking into account factors such as (i) growth of co-operative marketing in the commodity, (ii) introduction or proposal to introduce buffer stock schemes, (iii) monopoly procurement schemes, if any, in operation, (iv) introduction of a state distribution scheme, under which a portion of the commodity is distributed among consumers through the scheme, etc.

5. (a) Do you consider organisation of non-transferable specific delivery contracts, which are meant for giving and taking actual delivery of goods at a future date after a period of 11 days under the auspices of an association necessary ?

(b) If not organised, what steps would you suggest to prevent their misuse for conducting futures or hedge trading when futures or hedge trading in the concerned commodity is not permitted?

(c) In certain essential commodities, such as foodgrains, edible oilseeds and oils, facilities for trading in these ntsd contracts have been prohibited or suspended in view of their possible misuse and also relative shortage of the total supply. Has this affected the efficient marketing of these commodities in any way ?

(d) Would you suggest regulation of these contracts as a rule under section 15 of the FC(R) Act through recognised associations ?

6. (a) Ready delivery contracts, which are performed within a period of 11 days, are outside the purview of the FC(R) Act, 1952. Do you think that some form of regulation and control over ready contracts is necessary to achieve the broad objective of regulation of forward contracts under the FC(R) Act ?

(b) Do you think that leaving out ready delivery contracts in a commodity from any sort of control is likely to come in the way of effective regulation of forward contracts in the commodity ?

(c) If you think that some control over ready delivery contracts is necessary, what type of control would you suggest? Please give full justification.

Utilization of facilities by different functional interests

7. What is the extent to which the various functional interests viz., growers/producers, ready stockists, dealers, crushers, processors, exporters, importers, industrial consumers, etc. make use of the facility of forward trading at present, or used such facilities when such trading was permitted at your Association ? A detailed write up on this aspect may please be furnished supported by statistical data wherever possible.

Effects of forward trading

8. In the light of your experience of futures trading in the concerned commodities during the last 10 years, can it be said that futures trading has a steadying effect on the prices of the commodity and that it reduces the magnitude of seasonal fluctuations by graduating the fall in prices during the peak marketing period and rise in prices during the lean marketing period as generally contended ? Please support your contention, if in the affirmative, by statistical evidence.

9. (a) Please give an account of the relationship that existed between the ready and futures prices in respect of the commodity traded at your Centre.

(b) The monthly normal carry-over charges (cost of storage, interest, insurance, etc.) may also please be stated indicating the extent to which they get reflected in the futures price quotations with reference to ready prices.

(c) What provisions in the bye-laws of the recognised association and other conditions for trading would you suggest to assure that ready and futures prices move together and bear proper relationship to each other ?

10. (a) Do you think that forward trading serves as a reliable indicator of the likely trend of futures prices reflecting the expected supply and demand situation for the future period for which such prices are quoted ?

(b) Does it help different functionaries in the concerned commodities to plan their economic activities over time ? Please explain this aspect in detail by illustration and giving evidence, if any.

Benefit to growers and consumers

11. (a) Do the growers/producers make use of the facility of forward trading ?

(b) Which types of forward contracts they generally use ?

(c) If possible, mention the number of growers/producers utilising the facility directly and the extent of their participation in such trading at your Association.

(d) Please indicate the nature and extent of the benefits actually derived by them.

(e) If the growers/producers do not directly participate in forward trading at your association, do they derive any benefit from forward trading indirectly ? If so, please explain the nature of and the process through which the benefits accrue to them.

(f) Have you any suggestions to make regarding the location of recognised futures markets with a view to extending their benefits to the growers of the concerned commodities.

12. To what extent forward trading is beneficial to the final consumers of the commodity ? Give details.

13. Does forward trading help in eliminating gluts during peak period of arrivals and ensuring better availability during the lean period, thereby ensuring a more even supply of the commodity during the season as a whole ? Please indicate your experience with reference to the commodities with which you are concerned.

Benefits to exporters/importers

14. (a) Do the exporters /importers make use of the futures market for hedging purposes ? If so, which are the commodities in which such facilities will be of use to the exporters/importers and which are the commodities in which the facility is demanded by the exporters/importers ?

(b) What is the actual manner in which exporters/importers make use of the futures market for hedging their export sales/import purchases ?

(c) Can the futures markets functioning in foreign countries be of use to our importers ? If so, please explain the manner in which such facilities can be utilised by them and be beneficial to them.

(d) Do you think that in the absence of the facility of futures trading the exporter/importer will be handicapped in effecting export sales/import purchases in the required quantum and on his competitive ability ? Please give a detailed account of your views in this regard.

(e) Has forward trading still a role to play in the context of the policy of canalisation of exports/imports through State Agencies in certain commodities ? Can forward trading play a useful role even in respect of certain commodities the exports/imports of which have been canalised ? Explain your views in detail with illustrations.

(f) What are the other types of forward contracts used by exporters/importers and how ?

Regulation

15. The FMC has over time evolved a number of regulatory measures to enable the Boards of recognised associations and the Commission to ensure orderly conduct of forward trading, curb excessive speculation and its effects on prices, prevent manipulation, payment crisis, etc. These important measures are :

(i) Limit on price fluctuations ;

(ii) Limit on open position ;

(iii) Imposition of special margins on sales/purchases ;

(iv) Postponement of outward payment in respect of periodical clearing ;

(v) Fixation of maximum/minimum prices ;

(vi) Prohibition of fresh trading to ensure orderly settlement of standing open position ;

(vii) Shortening or lengthening the duration of ntsd contracts.

One or suitable combination of these measures is introduced by the recognised associations or the Commission if the situation so warrants.

(a) Do you think that these regulatory measures are adequate and have the desired effects ? If not what alternative or additional measures would you suggest to ensure that operations on forward markets in the commodities in which such trading is allowed are conducted on sound and proper lines and help in maintaining prices within reasonable limits.

(b) Sometimes, introduction of regulatory measures in recognised forward markets results in diversion of trading to unofficial channels. What measures would you suggest to deal with such situations? In what way the regulation could be strengthened?

(c) In order to make the regulatory measures introduced in respect of forward markets effective, do you consider introduction of similar or other measures simultaneously in the ready market in the commodity also necessary ? If so, what types and forms of regulatory measures would you consider suitable and what powers should be vested in the Forward Markets Commission for the purpose.

Efficient enforcement of the Act

16. Do you consider the existing scheme of the Forward Contracts (Regulation) Act viz., regulating forward trading in certain commodities in which such trading is considered necessary under section 15 of the Act, prohibiting forward trading in the commodities in which such trading is not considered desirable under section 17 of the Act and leaving other commodities free for party to party contracts but requiring organised forward trading in such free commodities to be conducted under associations registered under the Act adequate to achieve the efficient management of forward trading ? If not, what alternative schemes or amendments would you suggest to ensure better management of forward trading ?

17. Are the present provisions in the Act to deal with illegal forward trading sufficient to check such trading when prohibited under the Act ? If not, what amendments would you suggest to check more effectively such illegal forward trading ?

18. Under the present scheme of the Forward Contracts (Regulation) Act, when forward trading is regulated under section 15 of the FC (R) Act, every forward contract for the sale or purchase of any commodity brought under section 15 entered into otherwise than between members of a recognised association or through or with any such member shall be illegal. In this scheme of regulation, the regulatory control directly covers only those who are members of a recognised association and not clients of the members if the clients are non-members. The members who trade

with or for non-members are made responsible for the obligations of the non-members. Do you consider this scheme satisfactory for the effective regulation and control over the operations of the non-members or do you consider any changes therein necessary ?

19. Do you consider it desirable to lay down that forward contracts in the commodities to which section 15 has been applied, should be permitted between members only so that every operator is a member of one of the recognised associations for the purpose ? If not, why and what alternatives would you suggest to have effective control over non-member operators ? Your views and suggestions in the matter may please be given in detail.

20. Do you think the present scheme of registration of every Association concerned with the regulation of forward trading in any commodity including the commodities to which the regulatory provisions have not been made applicable unnecessary ? If so, state the reasons.

C. List of Topics on which views of Individuals, Institutions, etc. were invited

1. Role of forward trading in the prevailing economic conditions and marketing/distribution systems in commodities in which such trading facilities are generally demanded.
2. Utility of forward trading from the point of view of producers, ready stockists, dealers, crushers, processors, industrial consumers, exporters, importers, etc. and the extent of such benefit that each sector would be able to secure.
3. Effects of forward trading on prices and on general economy.
4. Suggestions for amendment to the present Forward Contracts (Regulation) Act, 1952, for effective enforcement of the Act.
5. Suggestions for additional powers to the Forward Markets Commission for strengthening it to make futures trading socially purposeful.
6. Desirability of continuing the present arrangement of entrusting the responsibility of enforcing the provisions of the Forward Contracts (Regulation) Act, 1952, relating to illegal forward trading to the State Police in view of the highly technical nature of the offences.

ANNEXURE III

LIST OF THOSE FROM WHOM WRITTEN REPLIES WERE RECEIVED

I

Central/State Governments

1. The Ministry of Food, Agriculture, Community Development and Co-operation, Government of India, New Delhi.
2. Directorate of Cotton Development, Ministry of Food, Agriculture, Community Development and Co-operation, Department of Agriculture, Government of India, Bombay.
3. Directorate of Tobacco Development, Ministry of Agriculture and Irrigation, Department of Agriculture, Government of India, Madras.
4. Office of the Jute Commissioner, Ministry of Industry, Department of Industrial Development, Government of India, Calcutta.
5. Office of the Textile Commissioner, Ministry of Industry, Department of Industrial Development, Government of India, Bombay.
6. The Government of Gujarat, Gandhinagar.
7. The Government of Maharashtra, Bombay.
8. Food and Civil Supplies Department, Government of Maharashtra, Bomba
9. The Government of Tamil Nadu, Madras.
10. The Government of West Bengal, Calcutta.

II

Individuals

Delhi

1. Dr. G.S. Raychaudhuri, New Delhi.

Gujarat

2. Shri Dayaljibhai G. Patel, Surat.

Kerala

3. Shri K.N. Raj, Trivendrum.

Maharashtra

4. Shri B.N. Adarkar, Bombay.
5. Shri Pratap Bhogilal, Bombay.
6. Shri Vadilal Dagli, Bombay.
7. Shri V. Subramaniya Iyer, Bombay.
8. Dr. A.S. Naik, Bombay.
9. Shri G.S. Patel, Bombay.
10. Shri D.R. Pendse, Bombay.
11. Shri James Raj, Bombay.
12. Shri Madanmohan R. Ruia, Bombay.
13. Shri R.G. Saraiya, Bombay.
14. Shri R.D. Shah, Bombay.
15. Shri B.K. Sharma, Bombay.
16. Shri R.B. Vaghaiwalla, Bombay.
17. Shri E.K. Vasudevan, Bombay.
18. Prof. V.M. Dandekar, Pune.
19. Prof. S.V. Kogekar, Pune.
20. Shri Amritlal B. Kedia, Akola.

West Bengal

21. Shri K.P. Goenka, Calcutta.
22. Shri Matadin Khaitan, Calcutta.
23. Shri B.K. Swaika, Calcutta.

III

Institutions, Firms, Associations, etc.

Andhra Pradesh

1. Andhra Pradesh Cotton Association, Guntur.

Delhi

2. Delhi Vegetable Oil Traders Association, Delhi.
3. Federation of Indian Chambers of Commerce & Industry, New Delhi.
4. Indian Sugar Mills Association, New Delhi.
5. National Federation of Co-operative Sugar Factories Limited, New Delhi.

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Gujarat

6. The Ahmedabad Mill Owners' Association, Ahmedabad.
7. Gujarat Chamber of Commerce & Industry (Gujarat Vepari Mahamandal), Ahmedabad.
8. Shri Saurashtra Oil Mills Association, Jamnagar.

Karnataka

9. Karnataka Chamber of Commerce & Industry, Hubli.

Kerala

10. The Spices Export Promotion Council, Ernakulam.

Madhya Pradesh

11. The Central India Chamber of Commerce & Industry, Ujjain.

Maharashtra

12. All India Cottonseed Crushers' Association, Bombay.
13. The Bombay Bullion Association Ltd., Bombay.
14. The Bombay Oil Industries Pvt. Ltd., Bombay.
15. The Central Organisation for Oil Industry & Trade, Bombay.
16. The Cotton Buyers' Association, Bombay.
17. Cotton Corporation of India, Bombay.
18. The Cotton Textiles Export Promotion Council, Bombay.
19. Federation of Indian Art Silk Weaving Industry, Bombay.
20. The Groundnut Extractions Export Development Association, Bombay.
21. The Indian Cotton Mills Federation, Bombay.
22. The Indian Merchants Chamber, Bombay.
23. The Maharashtra State Co-operative Marketing Federation Ltd., Bombay.
24. Kilachand Devchand & Co. Pvt. Ltd., Bombay.
25. Premji Haridas & Co., Bombay.
26. Vegetable Oils Association of India, Bombay.

Tamil Nadu

27. The South India Cotton Association, Coimbatore.
28. The Tirupur Cotton Merchants Association, Tirupur.

West Bengal

29. The Bengal Chamber of Commerce & Industry, Calcutta.
30. Bharat Chamber of Commerce, Calcutta.
31. Bengal Oil Mills Association, Calcutta.
32. Gunny Trades Association, Calcutta.
33. Indian Chamber of Commerce, Calcutta.
34. Tea Board, Calcutta.

IV

Recognised Associations

Andhra Pradesh

1. The Adoni Oilseeds & Oil Exchange Ltd., Adoni.

Gujarat

2. The Ahmedabad Cotton Merchants Association, Ahmedabad.
3. The Ahmedabad Seeds Merchants Association Ltd., Ahmedabad.

4. Central Gujarat Cotton Dealers' Association, Broach.
5. The Saurashtra Oil and Oilseeds Association Ltd., Rajkot.
6. Southern Gujarat Cotton Dealers' Association, Surat.
7. The Surendranagar Cotton, Oil & Oilseeds Association Ltd., Surendranagar.

Kerala

8. The Alleppey Oil Millers' and Merchants' Association, Alleppey.
9. Cochin Oil Merchants' Association, Cochin.
10. India Pepper and Spice Trade Association, Cochin.

Madhya Pradesh

11. The Central India Commercial Exchange Ltd., Gwalior.
12. The Central India Cotton Association Ltd., Ujjain.

Maharashtra

13. The Bombay Oilseeds & Oils Exchange Ltd., Bombay.
14. The East India Cotton Association Ltd., Bombay.
15. The Grain, Rice & Oilseeds Merchants' Association, Bombay.
16. The Pepper & Ginger Merchants' Association Ltd., Bombay.
17. The Vanaspati Manufacturers' Association of India, Bombay.
18. The Madhya Pradesh Commercial Exchange Ltd., Akola.
19. The Shahupuri Forward Exchange Ltd., Kolhapur.
20. The Spices & Oilseeds Exchange Ltd., Sangli.

Punjab

21. The Indian Exchange Ltd., Amritsar.
22. The Ludhiana Grain Exchange Ltd., Ludhiana.
23. The Northern India Cotton Association Ltd., Bhatinda.

Tamil Nadu

24. The Madras Oil and Seeds Exchange, Madras.

Uttar Pradesh

25. The Agra Merchants' Chamber Ltd., Agra.
26. The Kanpur Commodity Exchange Ltd., Kanpur.
27. Vijai Beopar Chamber Ltd., Muzaffarnagar.

West Bengal

28. The East India Jute & Hessain Exchange Ltd., Galcutta.

V

Registered Associations

Haryana

1. The Jai Hanuman Trading Company Pvt. Ltd., Jind Mandi.

Madhya Pradesh

2. The Chamber of Commerce, Ratlam.
3. The Sindh Mahajan Exchange Ltd., Gwalior.
4. The Sukkur Mahajan Association Ltd., Gwalior.

Maharashtra

5. The Bombay Sugar Merchants Association Ltd., Bombay.
6. The Bombay Yarn Merchants Association & Exchange Ltd., Bombay.

7. Indian Oil & Produce Exporters Association, Bombay.
8. Vyapari Association, Sailu.
9. Wardha Merchants Association Private Ltd., Wardha.

Rajasthan

10. The Bullion Association Ltd., Jaipur.

Tamil Nadu

11. The Madras Kirana Merchants' Association, Madras.

Uttar Pradesh

12. The Baran Beopar Mandal Pvt. Ltd., Bulandshahr.

West Bengal

13. East India Oil Millers Association, Calcutta.
14. Indian Jute Mills Association, Calcutta.

ANNEXURE IV

LIST OF ASSOCIATIONS, FIRMS AND INDIVIDUALS WITH WHOM DISCUSSIONS WERE HELD

I. Bombay (30th and 31st May 1979)

1. The Indian Oil and Produce Exporters Association, Bombay.
   Shri R. Ruia.
   Shri T.H. Amersey.
   Shri H.R. Raja.
2. The Indian Vegetable Oil Export Association, Bombay.
   Shri M.L. Sawla.
   Shri T.J. Tanna.
   Shri V.G. Udeshi.
3. The Oils and Seeds Importers Association of India, Bombay.
   Shri E.A. Kadar.
   Shri G. Chandrashekhar.
4. Prominent Exporters of Castor Oil and Linseed Oil.
   (*i*) M/s. Jayant Oil Mills, Bombay.
   Shri V.G. Udeshi.
   (*ii*) M/s. Kilachand Devchand & Co. Pvt. Ltd., Bombay.
   Shri K.V. Shah.
   Shri P.M. Sanghvi.
   (*iii*) M/s. Premji Haridas & Co., Bombay.
   Shri Premji Velji.
   (*iv*) M/s. Bombay Oil Industries Pvt. Ltd., Bombay.
   Shri C.V. Mariwala.
   (*v*) M/s. Godrej Soaps Pvt. Ltd., Bombay.
   Shri K.R. Gokulam.
5. The Central Organisation for Oil Industry and Trade, Bombay.
   Shri H.H. Lillaney.
   Shri M.P. Mansingka.
   Shri R.C. Sheth.

6. Groundnut Extraction Export Development Association, Bombay.
   Shri C.V. Mariwala.
   Shri S.B. Jhaveri.
   Shri N.R. Vyas.
7. The Solvent Extractors Association of India, Bombay.
   Shri H.H. Lillaney.
   Shri G.V. Sirur.
   Shri B.M. Sheth.
8. The Bombay Oilseeds and Oils Exchange Ltd., Bombay.
   Shri Ramdas Kilachand.
   Shri Tulsidas Mulji Vishram.
   Shri Damji Doongarshi.
   Shri Premji Velji.
   Shri Khushalchand Sakarchand.
   Shri B.M. Shah.
9. The Ahmedabad Seeds Merchants Association Ltd., Ahmedabad.
   Shri Bansilal Mangaldas Shah.
   Shri Somchand Kalidas Shah.
   Shri H.C. Gandhi.
10. The Kanpur Commodity Exchange Ltd., Kanpur.
    Shri Nareshchandra Chaturvedi.
11. The Central India Commercial Exchange Ltd., Gwalior.
    Shri Tejmal Harkhawat.
    Shri Mulchand Jaisinghani.
    Shri Madan Gopal Agrawal.
    Shri Ghanshyamdas Khubchandani.
12. The State Trading Corporation of India Ltd., Bombay.
    Shri L.K. Vadehra.

II. Bombay (6th and 7th July 1979)

1. The Vanaspati Manufacturers' Association of India, Bombay.
   Dr. A.C. Chhatrapati.
   Shri Alok Joshi.
2. The Grain, Rice and Oilseeds Merchants' Association Ltd., Bombay.
   Shri Premji Bhanji.
   Shri Vasanji Lakhamsi.
   Shri Vasant Kumar Devji.
   Shri R.J. Bhatt.
3. The All India Cottonseed Crushers' Association, Bombay.
   Shri R. Naraindas.
   Shri K.T. Rajani.
   Shri A.N.Y. Rao.
4. The Jobbers and Staff Union of the Bombay Oilseeds Market, Bombay.
   Shri Harilal M. Parekh.
   Shri Radhesham Khandelwal.
   Shri Jugalkishore M. Shah.
5. The Cotton Corporation of India, Bombay.
   Shri N.S. Kulkarni.
   Shri V. Munikrishnan.

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6. The East India Cotton Association Ltd., Bombay.
   Shri Rajnikant Purushotam Shah.
   Shri Purushotam Jhunjhunwala.
   Shri D.G. Damle.
   Shri V.M. Unchagaonkar.
   Shri S.S. Barodia.
7. The Bombay Cotton Merchants and Mucadams Association Ltd., Bombay.
   Shri J.K.S. Nicholson.
8. The Cotton Buyers' Association, Bombay.
   Shri J.K.S. Nicholson.
9. Indian Cotton Mills Federation, Bombay.
   Dr. Mohanlal Piramal.
   Shri C.V. Radhakrishnan.
   Shri V.Y. Tamhane.
   Shri T.K.V. Aiyer.
10. The Mill Owners' Association, Bombay.
    Dr. Mohanlal Piramal
11. Dr. M.G. Pavaskar.
12. Prof. M.L. Dantwala.
13. Directorate of Cotton Development, Bombay.
    Shri K. Ramachandran.
    Shri L.S. Joshi.
14. Office of the Textile Commissioner, Bombay.
    Shri C. Shridharan.
    Shri S.R. Ray.
15. The Maharashtra State Co-operative Marketing Federation, Bombay.
    Shri N. Jayaraman.
    Shri N. Venkataraman.
    Shri B.H. Mody.

III. Calcutta (8th to 10th August, 1979)

1. The Gunny Trades Association, Calcutta.
   Shri Mulji K. Shroff.
   Shri Brijmohan Kalanauria.
   Shri Kamal G. Tulsidas.
   Shri Harilal C. Shah.
2. The Calcutta Jute Fabrics Shippers' Association, Calcutta.
   Shri L.G. Toolsidas.
   Shri A. Huq.
3. The office of the Jute Commissioner,
   Government of India,
   Calcutta.
   Dr. P.B. Dey.
4. The Jute Corporation of India Ltd., Calcutta.
   Shri S.K. Bhattacharya.
   Shri C. Radhakrishnadas.
5. Government of West Bengal.
   Shri A.K. Sen—Chief Secretary to the Government of West Bengal,

Shri T.C. Dutt—Secretary, Agriculture Department.
Miss R. Mazumdar—Secretary, Commerce & Industries Department.
Shri M.G. Kutty—Secretary, Finance Department.
Shri S.S. Dutta—Secretary, Food & Civil Supplies Department.
Shri L.B. Mondal—Director of Agriculture (Marketing).
Shri H.L. Mazumdar—Inspector, Enforcement Branch.

6. The East India Oil Millers' Association, Calcutta.
Shri H.P. Gupta.
Shri S.B. Bajoria.
Shri S.C. Chatterjee.
Shri Rajaram Mussadi.

Indian Jute Mills Association, Calcutta.
Shri S.N. Mundra.
Shri N.C. Mekani.
Shri T.C. Chaudhuri.
Shri S. Ghosh.
Shri Rameshwar Agarwal.
Shri M.D. Poddar.
Shri S.P. Chanda.

8. The East India Jute & Hessian Exchange Ltd., Calcutta.
Shri B.K. Dalmia.
Shri G.A. Bhatia.
Shri B.L. Kheruka.
Shri S.N. Bagla.
Shri M.L. Sharma.

9. The India Chamber of Commerce, Calcutta.
Shri P.K. Kanoria.
Shri B.N. Patodia.
Shri P.K. Sen.

10. The Bharat Chamber of Commerce, Calcutta.
Shri H.P. Gupta.
Shri B.K. Gupta.
Shri V.S. Agarwala.
Shri M.L. Patodia.
Shri S.C. Chatterjee.

11. Shri B.K. Swaika.

IV. Ahmedabad (8th and 9th October, 1979)

1. The Ahmedabad Cotton Merchants' Association, Ahmedabad.
Shri Gautambhai Shakarchand Shah.
Shri Himatbhai Shah.
Shri Narendrabhai Shah.
Shri Nawinbhai Shah.

2. The Central Gujarat Cotton Dealers' Association, Vadodara.
Shri Narendrakumar R. Rungta.
Shri Gajendrabhai H. Shah.
Shri Haribhai R. Patel.
Shri B.P. Trivedi.
Shri J.B. Amin.

3. The Southern Gujarat Cotton Dealers' Association, Surat.
   Shri Vrajilal B. Patel.
   Shri Jayantilal P. Kapali.
4. The West India Cotton Association Ltd., Ahmedabad.
   Shri Narottamdas Narandas Patel.
   Shri Somchand Kalidas Shah.
   Shri Iswarlal Bechardas Patel.
5. Shri Dakshin Gujarat Sahkari Cotton Marketing Union Ltd., Surat.
   Shri Vrajilal Babubhai Patel.
   Shri Dharmendrasinh Hamirsinh Vansadia.
6. The Gujarat State Co-operative Cotton Marketing Federation Ltd., Ahmedabad.
   Shri P.H. Bhatt.
   Shri S.M. Patel.
7. Gujarat Chamber of Commerce and Industry (Gujarat Vepari Mahamandal) Ahmedabad.
   Shri Bhikhoobhai N. Shah.
   Shri Jagdishbhai Manubhai.
   Shri L.V. Dani.
   Shri I.N. Kania.
8. The Ahmedabad Seeds Merchants Association Ltd., Ahmedabad.
   Shri F.N. Sanghavi.
   Shri S.K. Shah.
   Shri H.C. Gandhi.
9. Government of Gujarat.
   Shri H.K.L. Capoor—Chief Secretary to the Government of Gujarat.
   Shri S.H. Jagada—Secretary, Civil Supplies Deptt.
   Shri G.C. Baveja—Principal Secretary, Finance Deptt.
   Shri Joshi—Registrar, Co-operation.

V. Rajkot (10th October, 1979)

1. The Saurashtra Oil and Oilseeds Association Ltd., Rajkot.
   Shri G.B. Shivdasani.
   Shri H.C. Patel.
   Shri R.P. Shah.
   Shri J.B. Patel.
   Shri L.T. Mehta.
   Shri C.S. Mehta.
   Shri H.R. Chitalia.
   Shri J.M. Bavishi.
   Shri S.H. Parekh.
   Shri D.M. Vora.
   Shri T.L. Bhedi.
   Shri N.G. Shah.
   Shri P.R. Bharatiya.
2. The Rajkot General Merchants and Commission Agents Association, Rajkot.
   Shri R.L. Vithalan.
3. Grower from Saurashtra.
   Shri R.D. Patel.
4. The Surendranagar Cotton, Oil and Oilseeds Association, Surendranagar.
   Shri J.M. Bavishi.
   Shri D.M. Vora.
   Shri Jayantilal A. Shah.

VI. Delhi (30th and 31st October and 2nd November, 1979)

1. Vijay Beopar Chamber Ltd., Muzaffarnagar.
   Shri Hardwari Lal.
   Shri Ramchand Kalra.
2. The Agra Merchants Chamber Ltd., Agra.
   Shri Sohanlal Bansal.
   Shri Ramnath Agarwal.
3. The Indian Exchange Ltd., Amritsar.
   Shri Joginder Singh.
4. The Ludhiana Grain Exchange Ltd., Ludhiana.
   Shri Banarsi Dass.
   Shri Sardarilal Sud.
5. The Rohtak Krishna Trading Co. Ltd., Rohtak.
   Shri Jag Mohan Mittal.
6. The Hansi Punjab Commercial Exchange Ltd., Hansi.
   Shri Dalip Singh.
   Shri Puranmal.
   Shri S. S. Jain.
7. The Bhatinda Om Oils Exchange Ltd., Bhatinda.
   Shri Roshanlal.
   Shri Ramlal.
8. The Mahesh Beopar Bhandar Co. Ltd., Dhuri.
   Shri Hukam Chand.
   Shri Shankardas Jindal.
9. The National Federation of Co-operative Sugar Factories Ltd., New Delhi.
   Shri B. Gowda.
   Shri N.S. Jain.
   Shri S. Kumaraswamy.
   Shri P.K. Roy.
10. The Indian Sugar Mills Association, Delhi.
    Shri V.L. Dutt.
    Shri D.R. Dani.
    Shri J.S. Mehta.
    Shri S.L. Jain.
11. Delhi Vegetable Oils Traders Association, Delhi.
    Shri Hotchand Bhojumal.
    Shri Kharatilal Jain.
    Shri Sushil Kumar Pawa.
    Shri Jayaram.
12. Dr. G.S. Raychaudhuri,
    Delhi School of Economics, University of Delhi.
13. Shri S.S. Marathe—Secretary to the Government of India, Ministry of Industry, Delhi.
14. Dr. M.S. Swaminathan—Secretary to the Government of India, Ministry of Agriculture, Delhi,
    Dr. W.B. Donde—Economic & Statistical Adviser.

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VII. Cochin (27th and 28th December, 1979)

1. India Pepper and Spice Trade Association, Cochin.
   Shri Tharanath Shet.
   Shri M.L. Parekh.
   Shri M. Michael.
   Shri M.V. Khona.
   Shri S. Suriyanarayanan.
2. The Spices Export Promotion Council, Ernakulam, Cochin.
   Shri P.N. Shah.
3. The Tea Trade Association, Cochin.
   Shri O.R.M. Prabhu.
   Shri N.K. Rajan.
4. The South India Cotton Association, Coimbatore.
   Shri V. Ganeshan.
5. The Andhra Pradesh Cotton Association, Guntur.
   Shri M. Venkateswarlu.
6. The Cochin Oil Merchants Association, Cochin.
   Shri Devshi Bhanji Khona.
   Shri Kailash Gupta.
   Shri M.C. Varghese.
7. The Alleppey Oil Millers & Merchants Association, Alleppey.
   Shri E. K. Varghese.
   Shri A. K. Abdul Azeez Labba.
   Shri T. S. Subramonyam.
   Shri S. Krishna Iyer.
8. The Madras Oil and Seeds Exchange, Madras.
   Shri T. R. Thambu Reddi.

VIII. Trivandrum (29th December, 1979)

Government of Kerala.

Shri S. Ananthakrishnan—Chief Secretary to the Government of Kerala.
Shri Madhava Menon—Civil Supplies Commissioner & Special Secretary, Department of Food.
Shri C. K. K. Panicker —Additional Secretary, Department of Home.
Shri K. S. Nair —Additional Secretary, Department of Industry.
Shri P. Suseelan —Additional Director (Commercial Crops).
Shri N. Krishanan Nair —Agricultural Marketing Officer.
Shri P. Velappan Nair —Dy. Secretary, Deptt. of Agriculture.
Shri Varghese Vaidyan —Chairman, Coconut Development Corporation.

IX. Bombay (31st December, 1979 and 1st January, 1980)

1. The Bombay Yarn Merchants Association and Exchange Ltd., Bombay.
   Shri D. M. Barodia.
   Shri C. C. Parekh.
2. Federation of Indian Art Silk Weaving Industry, Bombay.
   Shri I. P. Poddar.
   Shri R. K. Batnagar.
   Shri D. A. Joshi.
   Shri K.A. Samuel.

3. The Madhya Pradesh Commercial Exchange Ltd., Akola.

Shri Narayan Dasji Khandelwal.
Shri Amaritlalji B. Kedia.

4. The Central India Cotton Association Ltd., Ujjain.

Shri Kantilal Jhalani.
Shri Shriniwas Ladha.
Shri M. M. Jain.

5 Government of Maharashtra, Bombay.

Shri P.G. Gawai—Chief Secretary to the Government of Maharashtra.
Shri P.G. Salvi—Secretary, Home Deptt.
Shri V. Prabhakaran—Special Secretary, Finance Department.
Shri V. Srinivasan—Secretary, Agriculture Deptt.
Shri M. Subramaniam —Secretary, Co-op. Deptt.
Shri D.M. Sukhtankar—Secretary, Industries, Energy and Labour Deptt.
Shri R.L. Paradeep—Secretary, Revenue & Forest Deptt.
Shri V. Venkatesan—Secretary, Planning Department.
Shri V.S. Gopalakrishnan—Managing Director, Maharashtra State Co-operative Marketing Federation.
Shri P.B. Khadikar—Managing Director, Maharashtra State Oilseeds Corporation.
Shri S.M. Kuray—Director of Marketing.
Shri S. Ramkrishna—Commissioner for Co-operation and Registrar of Co-operative Societies.
Shri S.R. Chopde—Director of Agriculture.
Shri V.D. Mahajan—Director, Economics & Statistics.
Shri B.N. Bhagwat—Industries Commissioner.

6. The Bombay Bullion Association, Bombay.

Shri Shantilal Sonawala.
Shri Makkanlal Damani.
Shri P.P. Dholakia.

7. The Spices and Oilseeds Exchange Ltd., Sangli.

Shri U.K. Shah.
Shri B.P. Nemani.
Shri N.K. Kulkarni.
Shri A.B. Deshpande.

8. The Grain Rice and Oilseeds Merchants Association Ltd., Bombay.

Shri Premji Velji Lakhamsi.
Shri Vasanji Lakhamsi.
Shri Premji Bhanji.
Shri Vasantkumar Devji.
Shri Maganlal Karamshi Vora.
Shri J.D. Parekh.

9. The Shahupuri Forward Exchange Ltd., Kolhapur.

Shri S.T. Patane.
Shri D.L. Shah.

X. Delhi (18th January, 1980)

1. Shri A.S. Gill—Secretary to the Government of India, Department of Commerce, Delhi.

Shri P.K. Kaul—Additional Secretary to the Government of India, Department of Commerce, Delhi.
Shri M.L. Kapoor—Joint Director.

XI. Delhi (7th February, 1980)

1. Shri G. Ramachandran—Secretary to the Govt. of India, Ministry of Finance, Delhi.

   Dr. Manmohan Singh—Secretary to the Govt. of India, Department of Economic Affairs, Delhi.

XII. Bombay (7th April, 1980)

1. The Pepper & Ginger Merchants Association, Bombay.

   Shri Dhirajlal M. Gandhi.
   Shri Vardhaman V. Khona.
   Shri D.N. Shah.

2. The Bombay Mudi Bazar Kariana Merchants Association, Bombay.

   Shri Ambalal I. Patel.
   Shri Purushottamdas D. Dattani.
   Shri Dineshchandra J. Khimasia.
   Shri M.P. Oza.

3. Shri D.R. Pendse.

ANNEXURE V

TYPICAL FUTURES OR HEDGE CONTRACTS

A typical 'Futures or Hedge Contract' framed for trading in castorseed at the Bombay Oilseeds and Oils Exchange Ltd., is given below :

Basis of the Contracts

(*i*) For the purpose of hedging there shall be a hedge contract in castorseed ;

(*ii*) The basis of quality of contract for castorseed will be 'Bombay Small Castorseed' ;

Other tenderable varieties

(*iii*) In the hedge contract, qualities tenderable against the basis quality shall be as under :

(*a*) Madras Small ;

(*b*) Gujarat Small ;

(*c*) Kutch and Saurashtra Small, and

(*d*) Castorseed Bold (including Kanpur Bold).

(*iv*) The Board may, in consultation with the Forward Markets Commission, add or delete or alter any qualities tenderable against the basic quality before the start of trading for the year. No change will be made therein for that year ;

Tendering differences

(*v*) The Board shall, before the start of trading for a particular year, fix differences, if any, payable by any parties to the contract for tendering different qualities against the basic quality and no change shall be made in the tenderable differences so fixed for the contracts of that year ;

Months of delivery

(*vi*) For castorseed the months of delivery shall be March, June and September ;

Delivery period and tender days

(*vii*) Delivery period shall be from the 1st to the last date of the month as provided in the bye-laws relating to tenders and delivery order. The first and the last working day of each delivery month and every Tuesday, Thursday and Saturday between these days (except when such day falls on a holiday fixed by the Board or a settlement day) shall be known as Tender Days ;

Unit of trading

(*viii*) The unit of transactions in the hedge contract shall be 5 metric tonnes ;

Unit of quotation

(*ix*) The unit of quotation in the hedge contract of castorseed shall be 100 kgs.

Commencement of trading

(*x*) Hedge trading in a new delivery will commence in the month of June or July for March and June deliveries of the following year and in the month of March for September delivery of the same year.

(*xi*) The upcountry centres at which delivery of castorseed is permitted will be as per schedule appended to the Bye-laws. The Board of Directors in consultation with the Forward Markets Commission may make such changes in the schedule as they think proper before the start of hedge trading for a particular year. No change will be made therein for that year.

Schedule of upcountry centres for delivery of Castorseed against hedge contracts

1 Veraval	16 Pendapalli	31 Kanpur
2 Jamnagar	17 Hyderabad	32 Kalpi
3 Navlakhi	18 Harij	33 Kaunch
4 Bedi	19 Patan	34 Mauranipur
5 Kandla	20 Unjha	35 Banda
6 Jadcharla	21 Visnagar	36 Karvi
7 Bhongir	22 Bhabhar	37 Bhind
8 Warangal	23 Kalol	38 Chanda
9 Shednagar	24 Talod	39 Balotra
10 Khamameth	25 Dohad	40 Gandhidham
11 Jangam	26 Sidhpur	41 Agra
12 Raichur	27 Ahmedabad	42 Allahabad
13 Falaknama	28 Vijapur	43 Samastipur
14 Nizamabad	29 Chanasma	44 Begusarai
15 Mancherial	30 Deesa	45 Sitapur

ANNEXURE VI

PROCEDURE OF ENTERING INTO A FUTURES CONTRACT

The procedure of entering into a futures contract is illustrated below :—

A non-member trader, say a crusher of castorseed, decides on the 5th July 1979 to purchase 100 tonnes of castorseed in a Futures Contract, when trading is being carried on in September 1979 and April 1980 futures contracts under a recognized association. The non-member trader (crusher client) selects to trade in September Contract and orders his broker, who is a member of the association, to buy 100 tonnes castorseed in September at the market rate, i.e. at the going price at the time the order reaches the floor of the association. The order is transmitted in a few minutes, often in a few seconds, to the broker's representative in the ring and is immediately executed with another trader (member or non-member) or another broker member of the association, who has a similar order to sell September castorseed. The order is executed at a price of Rs. 250 per quintal.

Thus, the standard September castorseed Contract has been entered into by a buyer, who has promised to purchase 100 tonnes of castorseed in September at Rs. 250 per quintal, the total purchase price being Rs. 2.5 lakhs. The seller of the contract has made a similar agreement to deliver castorseed sometime during September at the same price. Neither party has had to advance as yet either the castorseed or Rs. 2.5 lakh, representing the cost of the contract. Each has had often to provide a margin, probably about 5 to 10 per cent depending upon the rates prescribed by the association to signify his good faith and intention to carry out the agreement. If delivery takes place, the remainder of the purchase price will be advanced by the buyer. If delivery does not take place, no additional funds will be required. The buyer does not yet own any castorseed and the seller may or may not own any. The buyer anticipates that the price of castorseed is likely to go up before September and he has thus taken a "long" position in the Futures market. The seller may actually have castorseed that he plans to deliver on the contract, or he may be hedging his purchase of actual castorseed, or he may be expecting that the price of the castorseed will decline and that he can buy back his contract at a lower rate; in that case, he would be taking a "short" position in the futures market by promising to sell something that he does not yet possess but which he can acquire prior to the last date provided for settlement of the contract by actual delivery.

If both the parties keep their contract open until September, delivery of castorseed may take place. Trading in the September future will continue upto a date fixed by the association, usually around 25th September. But notices

of delivery may be issued by sellers, right on the first day of the delivery month (i.e. September) and on the subsequent prescribed days (called tender days). If delivery is offered by the seller prior to the close of trading in the September futures contract, the buyer may either accept delivery or he may sell his futures contract and retender the delivered castorseed to another trader. Contracts held open after the last tender day are normally squared up at an appropriate rate called 'due date rate' at the end of the month.

In practice most futures contracts are not settled by delivery of the commodity. Rather, an evening out process takes place whereby buyers sell their contracts and sellers buy back contracts at different times and with different parties. The parties to the original contract can be relieved of their obligations with ease, as the associations organising futures trading facilities maintain a clearing house, somewhat similar to that maintained for settlements among banks, to keep tract of long and short positions and to determine who are the parties to contracts at any given time. The clearing house of a futures association recognises only members as principals. It does not deal directly with clients or non-members. The association requires every member to report to its clearing house all purchases and sales every day or at the end of a week (depending on whether the 'clearing' is daily or weekly). The Clearing House collects amount payable by the members in respect of their outstanding trading positions on the basis of the extent to which the price of the concerned futures contract has moved against them and pays the amounts to the members in whose favour the price has moved. This clearing house procedure prevents accumulation of any large scale financial risk and facilitates liquidation of outstanding position by members without any financial risk to the opposite parties involved. It is likely that neither party intended delivery at the time the contract was made. The futures market is not a market for purchasing actual commodity, since the buyer cannot prescribe the quality and specifications of his choice.

ANNEXURE VII

ILLUSTRATIONS OF HEDGING

The nature of hedging and its outcome is illustrated in the following examples.

The selling hedge (selling futures) is used to protect against possible price fall by stockists and manufacturer who own commodities. The buying hedge (a purchase of futures) is used to protect against possible price increase of the actual commodity by exporters, users of commodity, etc.

The selling hedge

Suppose on 1st January, 1979, a stockist in the interior purchases from a producer 100 tonnes of castorseed on the basis of the price prevailing at the nearest terminal market, Ahmedabad, say at Rs. 250 per quintal. He would pay to the producer after making deductions for handling, freight, expected storage insurance and his expected merchandising charge or renumeration. (The price that he pays to the producer would also depend upon whether or not he would be able to insure against the price fluctuation that may take place between the time of his purchase and the time of his sale of the stock). If he does not wish to speculate in the hope that the expected price fluctuation over time till he disposes of his stock may be in his favour, but desires to insure against the risk in case the price fluctuation is against him, he may hedge his stocks in a suitable futures market at say Ahmedabad if there is such a market at the centre and lift his hedge immediately on the day he is able to sell his castorseed say to a crusher. This hedging operation can be described as follows :

Date		Ready transaction		Hedge April 1979 delivery transaction	
		Quantity	Price per quintal	Quantity	Price per quintal
1st January	..	100 tonnes purchased	Rs. 250	100 tonnes sold	Rs. 255
1st April 1979	..	100 tonnes sold	Rs. 245	100 tonnes purchased back	Rs. 250
Profit or loss	..		loss of Rs. 5 per quintal		gain of Rs. 5 per quintal

The buying hedge

Suppose a crusher-exporter sells 100 tonnes B.S.S. castorseed oil to a foreign buyer for export at a fixed price of Rs. 7,605 per tonne ($951.00) for three months later, when indigenous corresponding oil is being sold in the country for Rs. 6,550. To protect himself against a possible price increase, he would have preferred to purchase castorseed oil futures. However, if futures trading is not permitted in castorseed oil but in castorseed (as was the case in India), he would use castorseed futures and use castorseed prices for the purpose of his calculations[1] as follows :—

Date	NTSD/READY Transactions in castor oil (B.S.S.)					Hedge April 1979 delivery transaction in castorseed	
	Quantity of oil	Price per tonne		Equivalent quantity of seed	Prices per quintal	Quantity	Price per quintal
		Foreign market	Indigenous market				
1-1-79 ..	100 tonnes (sold for delivery in April)	$951 (Rs. 7,605)	Rs. 6,550	250 tonnes	Rs. 250	250 tonnes (purchased)	Rs. 255
1-4-79 ..	100 tonnes (purchased)	$967 (Rs. 7,736)	Rs. 6,680	250 tonnes	Rs. 255	250 tonnes (sold)	Rs. 260
Profit or Loss ..					Loss of Rs. 5 per quintal		Gain of Rs. 5 per quintal

[1]. For details of these calculations see Table on page 90.

Though the avoidance of price risks is normally considered as the motivation for hedging, Prof. Holbrook Workings has made some finer distinctions between different types of hedging and as a consequence, by and large, the following types of hedging are recognised in the recent literature.

(i) **Routine hedging**—This type of hedging relates to the hedging of price risks as explained above, which involves the routine 'covering' of the trader's position in actuals by entering into equivalent off-setting transactions in futures. This type of routine hedging is accepted as a standard practice.

Routine (short) hedging is attractive to a trader, processor or manufacturer, whose main business activities require the holding of stocks, but who is unwilling to trust his judgement about prospective price movements.

(ii) **Selective or discretionary hedging**—This type of hedging is distinguished from routine hedging, by the excercise of judgement about price changes by the trader. A selective short hedger is one who practices hedging only when he strongly expects a fall or a rise in the prices. On other occasions, he speculates with his stocks. His decision to hedge the whole or part of his stocks depends upon his confidence in his own judgement regarding future course of prices, his financial resources and his ability to withstand losses.

(iii) **Arbitrage or carrying charge hedging**—The third type of hedging called 'arbitrage' hedging is practised to take advantage of expected favourable changes in the 'spread' between the ready and futures prices or between the prices of different futures contracts, whereas the first two (routine and selective) types of hedging are carried out in response to the uncertainty about price changes.

(iv) **Anticipatory hedging**—In this case, the sale or purchase of futures contracts is made before the actual commitments are entered into. "The anticipatory hedge serves as a temporary substitute for a merchandising contract that will be made later". However, since there is no simultaneity or near simultaneity between the future and actual transactions, this use of futures market, though may prove beneficial to the party concerned, has to be treated on par with speculation, as till the actual commitment is made, the distinction between the so called anticipatory hedge contract and speculative contract is merely in the motives of the operator.

TABLE

PART I

Castor Oil prices to be worked out on the basis of castorseed Prices

(in Rs.)

Price of castorseed (per 100 kg.)	250.00	255.00
Sales tax 4%	10.00	10.20
	260.00	265.20
Castorseed per tonne	2600	2652
Price for 2½ tonnes	6500	6630
Addl. crushing charges @ Rs. 125 per tonne for 2½ tonnes	312.50	312.50
	6812.50	6942.50
Deduct		
Price of cake for 1½ tonne @ Rs. 575 per tonne	862.50	862.50
	5950.00	6080.00
Add		
As expenses to convert commercial oil into B.S.S. per tonne	600.00	600.00
	6550.00	6680.00
Parity Price for B.S.S. Oil in internal market	6550	6680

PART II

Castor Oil Prices at Rotterdam to be worked out on the basis of castor oil prices at Bombay

	Seed price per quintal : Rs. 250.00	Rs. 255.00
	B.S.S. Castor oil	B.S.S. Castor oil
Oil price per tonne	6550	6680
Add (F.O.B. charges i.e. handling, agmarking, loading, B.P.T. clearing-forwarding exp.)	200	200
	6750	6880
Add Freight ($80)	625	625
Rotterdam 1% insurance	74	75
	7449	7580
Add Expenses Rotterdam ($20) Forwarding C.I.F.	156	156
Parity price in Rotterdam (Rs. 8.00=$1)	Rs. 7605	Rs. 7736

NOTE : These price calculations take into account normal profit margins of crusher-exporters.

ANNEXURE VIII

COMPARISON OF CO-EFFICIENTS OF VARIATION* FOR PERIODS WITH AND WITHOUT FUTURES TRADING IN DIFFERENT COMMODITIES

1. Cotton—BOMBAY

Figures of monthly cotton index deflated by average yearly general index

Season Sept—Aug.	With futures trading	Season Sept—Aug.	Without futures trading
1954-55	8.55	1966-67	3.31
1955-56	6.94	1967-68	4.84
1956-57	3.43	1968-69	4.85
1957-58	2.15	1969-70	7.41
1958-59	3.24	1970-71	9.71
1959-60	4.64	1971-72	16.39
1960-61	1.99	1972-73	15.11
1961-62	2.84	1973-74	11.14
1962-63	3.30	1974-75	12.40
1963-64	2.42	1975-76	17.16
1964-65	2.11	1976-77	2.53
1965-66	2.76	1977-78	3.62
		1978-79	1.48

$$\text{*Co-efficient of variation} = \frac{\text{Standard Deviation}}{\text{Actual Mean}} \times \frac{100}{1}$$

2. Groundnut—BOMBAY

Figures of monthly average prices of groundnut being deflated by yearly average of general index

Season (Nov—Oct)	With futures trading	Season (Nov—Oct)	Without futures trading
1956-57	4.83	1963-64 (June—Oct. '64)	6.34
1957-58	8.91	1964-65	11.51
1958-59	6.99	1965-66	13.68
1959-60	7.01	1966-67	12.15
1960-61	9.24	1967-68	13.31
1961-62	3.11	1968-69	15.12
1962-63	8.17	1969-70	7.17
1963-64 (Upto May 1964)	8.35	1970-71	4.77
		1971-72	10.18
		1972-73	16.36
		1973-74	6.85
		1974-75	7.82
		1975-76	19.93
		1976-77	13.35
		1977-78	5.95
		1978-79	15.89

3. Groundnut Oil—BOMBAY

Figures of monthly average prices of groundnut oil being deflated by yearly average of general index

Season (Nov—Oct)	With futures trading	Season (Nov—Oct)	Without futures trading
1958-59	5.53	1963-64 (June—Oct. 1964)	7.44
1959-60	7.93	1964-65	14.65
1960-61	6.99	1965-66	13.52
1961-62	3.33	1966-67	11.27
1962-63	6.19	1967-68	17.50
1963-64 (Nov—May 1964)	7.63	1968-69	15.68
		969-70	10.85
		1970-71	3.07
		1971-72	9.13
		1972-73	16.67
		1973-74	10.21
		1974-75	6.00
		1975-76	16.43
		1976-77	13.18
		1977-78	3.55
		1978-79	19.93

4. Coconut oil—COCHIN

Figures of monthly average prices of coconut oil being deflated by yearly average general index

Season (Nov.—Oct.)	With futures trading	Season (Nov.—Oct.)	Without futures trading
1958-59	3.07	1971-72	7.54
1959-60	5.00	1972-73	20.91
1960-61	5.57	1973-74	5.92
1961-62	9.22	1974-75	18.54
1962-63	5.92	1975-76	15.56
1963-64	3.98	1976-77	14.90
1964-65	16.25	1977-78	7.80
1965-66	8.13	1978-79	8.55
1966-67	10.21		
1967-68	10.94		
1968-69	10.15		
1969-70	10.11		
1970-71	13.20		

5. Hessian—CALCUTTA

Figures of monthly average prices of hessian being deflated by yearly average prices of hessian

Season July—June	With futures trading	Season July—June	Without futures trading
1958-59	3.03	1971-72	2.00
1959-60	7.81	1972-73	2.44
1960-61	12.69	1973-74	21.38
1961-62	5.66	1974-75	12.32
1962-63	6.48	1975-76	2.24
1963-64	2.82	1976-77	2.02
1964-65	7.81	1977-78	7.35
1965-66	6.16	1978-79	12.17
1966-67	4.24		
1967-68	3.46		
1968-69	6.78		
1969-70	6.48		
1970-71	7.35		

6. Cottonseed—AHMEDABAD

Figures of monthly average prices of cottonseed being deflated by yearly average prices of cottonseed at Ahmedabad

Season (Nov.—Oct.)	With futures trading	Season (Nov.—Oct.)	Without futures trading
1960-61	4.12	1971-72	11.17
1961-62	6.17	1972-73	15.79
1962-63	7.24	1973-74	6.81
1963-64	5.85	1974-75	12.20
1964-65	11.86	1975-76	17.21
1965-66	12.77	1976-77	7.55
1966-67	11.60	1977-78	10.65
1967-68	15.22	1978-79	10.45
1968-69	8.01		
1969-70	1.71		
1970-71	13.89		

7. Rapeseed/Mustardseed—KANPUR

Figures of monthly average prices of rapeseed/mustardseed being deflated by yearly average prices of rapeseed/mustardseed at Kanpur

Season (Nov—Oct)	With futures trading	Season (Nov—Oct)	Without futures trading
1960-61	8.22	1968-69	6.04
1961-62	7.04	1969-70	5.19
1962-63	3.54	1970-71	9.40
1963-64	9.99	1971-72	6.91
		1972-73	15.95
		1973-74	6.61
		1974-75	19.87
		1975-76	13.37
		1976-77	11.09
		1977-78	8.49
		1978-79	8.72

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ANNEXURE IX

PROVISOS ADDED TO THE DEFINITION OF READY DELIVERY CONTRACT IN THE FORWARD CONTRACTS (REGULATION) ACT, 1952 BY AMENDMENT MADE IN 1971

"Provided that where any such contract is performed either wholly or in part,—

(1) by tendering of the documents of title to the goods covered by the contract by any party thereto (not being a commission agent or a bank) who has acquired ownership of the said documents by purchase, exchange or otherwise, to any other person (including a commission agent but not including a bank); or

(2) by the realisation of any sum of money, being the difference between the contract rate and the settlement rate or clearing rate or the rate of any offsetting contract; or

(3) by any other means whatsoever, and as a result of which the actual tendering of the goods covered by the contract or the payment of the full price therefor is dispensed with, then, such contract shall not be deemed to be a ready delivery contract.

Explanation : For the purposes of this clause,—

(*i*) "bank" includes any banking company as defined in the Banking Regulation Act, 1949, a co-operative bank as defined in the Reserve Bank of India Act, 1934, the State Bank of India and any of its subsidiaries and any corresponding new bank constituted under section 3 of the Banking Companies (Acquisition and Transfer of Undertakings) Act, 1970;

(*ii*) "Commission agent" means a person who, in the ordinary course of business, makes contract for the sale or purchase of goods for others for a remuneration (whether known as commission or otherwise) which is determined in the contract itself or determinable from the terms of the contract, in either case, only with reference to the quantity of goods or to the price therefor as stipulated in the contract."

सत्यमेव जयते

ANNEXURE X

DETAILS OF THE RAIDS CONDUCTED AND CASES REGISTERED UNDER THE FORWARD CONTRACTS (REGULATION) ACT, 1952

(as on 31-3-19

S. No.	Year	Total No. of raids	Total No. of cases registered	Total No. of cases pending scrutiny	No. of cases in which no evidence found	%age of Col. No. 6 to Col. No. 4	No. of cases dropped	%age of Col. No. 8 to Col. No. 4	No. of cases in which evidence found	%age of Col. No. 10 to Col. 4	No. of cases pending investigation	%age of Col. No. 12 to Col. No. 10	No. of cases pending trial	%age of Col. No. 14 to Col. No. 10	No. of cases decided	No. of cases convicted	%age of Col No. 17 to Col. No. 16	No. of cases acquitted	%age of Col. No. 19 to Col. No. 16	No. of cases referred to recognised associations for disciplinary action
1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18	19	20	21
1	1957	4	5	—	—	—	2	40	3	60	—	—	—	—	3	1	34	2	66	—
2	1958	6	37	—	—	—	2	5	35	95	—	—	—	—	35	22	63	13	37	—
3	1959	10	20	—	—	—	2	10	18	90	—	—	—	—	18	15	83	3	17	—
4	1960	19	36	—	7	19	5	14	24	67	—	—	—	—	24	19	70	5	21	—
5	1961	12	56	—	7	12	1	2	48	86	—	—	—	—	48	42	87	6	13	—
6	1962	8	12	—	1	8	3	25	8	67	—	—	1	12	7	2	29	5	71	—
7	1963	14	19	—	2	11	—	—	17	89	—	—	—	—	17	10	59	7	41	—
8	1964	16	18	—		—	2	11	16	89	—	—	—	—	16	6	38	10	62	—
9	1965	21	50	—	7	14	7	14	36	72	—	—	2	6	34	18	53	16	47	—
10	1966	21	62	—	20	32	13	21	29	47	—	—	3	10	26	12	46	14	54	—
11	1967	28	81	—	13	16	8	9	60	74	—	—	2	3	58	31	54	27	46	—
12	1968	23	63	—	22	35	10	16	31	49	—	—	6	20	25	11	44	14	56	—
13	1969	32	49	—	7	14	9	18	33	68	—	—	6	18	27	10	37	17	63	—
14	1970	34	65	—	28	43	4	9	33	48	—	—	4	12	29	7	24	22	76	—
15	1971	41	102	—	52	51	4	4	46	45	—	—	15	33	31	11	36	20	64	—
16	1972	98	149	—	76	51	11	8	62	42	—	—	19	31	37	11	30	26	70	6
17	1973	72	108	—	65	60	4	3	39	36	—	—	14	36	25	3	12	22	88	—
18	1974	67	109	—	54	49	1	1	54	50	—	—	15	28	27	10	37	17	63	12
19	1975	71	108	—	47	44	2	2	59	54	—	—	32	54	23	10	45	13	57	4
20	1976	128	173	—	114	66	1	—	58	34	1	2	30	52	18	3	17	15	83	9
21	1977	126	161	—	94	59	2	2	65	40	1	1	48	74	14	7	51	7	49	2
22	1978	186	211	7	122	57	3	1	79	37	5	6	68	86	6	—	—	6	100	—
23	1979	172	186	57	91	49	4	2	34	18	22	65	12	35	—	—	—	—	—	—
24	1980 (upto (31-3-80)	30	34	27	7	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—
Total		1,239	1,914	91	836		100		887		29		277		548	261		287		33@

@NOTE :—Out of 33 cases, 25 cases (76%) have been decided by the Boards of recognised associations. Remaining 8 cases are still pending action. From 25 cases decided by the boards, punishment is awarded in 24 cases and 1 case is closed without awarding punishment.

ANNEXURE XI

DESIGNATED MARKETS FOR FUTURES TRADING AND COMMODITIES TRADED UNDER THEM IN THE U.S.A.

(as on September 30, 1978)

Markets	Commodities
1. Chicago Board of Trade (CBOT)	1. Wheat 2. Corn 3. Oats 4. Soyabeans 5. Soyabean Oil 6. Soyabean Meal 7. Iced Broilers 8. Silver 9. Gold 10. Plywood 11. GNMA's 12. GNMA-CD's 13. Commercial Paper 14. T-Bonds
2. Mid America Commodity Exchange (MACE) ..	1. Wheat 2. Corn 3. Oats 4. Soyabeans 5. Silver 6. Gold 7. Live Hogs 8. Live Cattle
3. Chicago Mercantile Exchange (CME)	1. Fresh Eggs 2. Idaho Potatoes 3. Turkeys 4. Live Cattle 5. Live Feeder Cattle 6. Live Hogs 7. Lumber 8. Stud Lumber 9. Frozen boneless beef 10. Frozen Pork Bellies 11. British Pound 12. Canadian Dollar 13. Deutsche Mark 14. Dutch Guilder 15. U.S. Silver Coins 16. Japanese Yen 17. Mexican Peso 18. Swiss Franc 19. French Franc

ANNEXURE XI—*contd.*

Markets	Commodities
	20. Gold
	21. Treasury Bills-90 day
	22. Treasury Bills-1 year
4. Kansas City Board of Trade (KCBT)	1. Grain Sorghum
	2. Wheat
5. Minneapolish Grain Exchange (MGE)	1. Durum Wheat
	2. Wheat
6. New York Mercantile Exchange (NYME)	1. Imported Boneless beef
	2. Maine Potatoes
	3. Rd White Potatoes
	4. Palladium
	5. Silver Coins
	6. Gold
7. New York Cotton Exchange (Cotton)	1. Cotton # 2
	2. Froz Con OJ
	3. Wool
	4. Propane
	5. Petroleum
8. New York Cocoa Exchange (Cocoa)	1. Cocoa
	2. Rubber
9. Commodity Exchange Inc (Comex)	1. Copper
	2. Silver
	3. Gold
	4. Zinc
10. New York Coffee and Sugar Exchange (NYC&S) ..	1. Sugar 11 & 12
	2. Coffee. C
11. Amex Commodities Exchange (Amex)	1. GNMA

Source : Annual Report of Commodity Futures Trading Commission 1978.

ANNEXURE XII

REGULATORY MEASURES ADOPTED BY THE FORWARD MARKETS COMMISSION

(*i*) **Special or automatic clearings**—These are clearings in addition to the periodical regular clearings whenever the closing futures price on any day varied from the previous clearing rate by more than a specified amount or a specified percentage. (Such clearings, requiring payment of amounts to the clearing house of the recognised association by the parties against whom the prices have moved, discourage operators from increasing their commitments unduly and also reduce the risk of defaults).

(*ii*) **Ordinary margins**—These are deposits paid by members on their outstanding (or open) contracts at the rates specified in the bye-laws and mainly serve as security against the risk of default arising from price fluctuation between two clearings.

(*iii*) **Special margins**—Special margins are introduced when futures prices are found to be moving sharply in only one direction and it is considered that the movement is not entirely justified by economic factors. In order to dissuade the buyers from increasing their purchases in times of continuous price rise or the sellers from increasing their sales

in times of continuous price fall, the buyers or the sellers as the case may be are called upon to pay these special additional deposits, whenever the prices rise above or fall below the prescribed futures price levels. As a consequence, the operators are expected to liquidate their unduly large holdings or at least to refrain from entering into further commitments.

(*iv*) **Postponement of outward payment**—Under this measure, the amounts to be paid by the clearing house as a result of the clearing to members who are to receive such amounts on account of the price having moved in their favour, are not paid for the time being. When the prices are moving in on direction and special margins are in operation, the incidence of the rate of special margin on an operator is reduced to the extent to which he is to receive the amount from the clearing house. Postponement of this payment by the clearing house, retains the effectiveness of special margin.

(*v*) **Limit on daily or weekly price fluctuations**—The limit on daily or weekly price fluctuation was imposed by the Commission mainly to stagger the one-way movement of the prices. As a result of this limit, operators in the futures market could not buy or sell in the futures market at a price higher or lower than the closing price of the previous day or of the last day of the previous week as the case may be by the amount of the limit fixed.

(*vi*) **Limit on open position**—When limits on open position are prescribed, the operator in the futures market is not allowed to hold or control an open position in excess of the prescribed limit. Such limits directly prevent the holding of large open positions and thus curb excessive speculation.

(*vii*) **Maximum and minimum prices**—Maximum and minimum prices are prescribed with a view to restricting the movement of the futures prices within the specified levels. When the prices touch the prescribed maximum or minimum level, futures trading in the commodity in the concerned delivery automatically comes to a standstill. If the prices remain at the maximum or minimum levels the outstanding contracts in the delivery are settled at the maximum or the minimum prices as the case may be.

(*viii*) **Prohibition of fresh trading**—When difficulties are anticipated in the smooth functioning of a future delivery, the operators are prohibited from entering into fresh transactions though they are permitted to offset their earlier outstanding purchase or sale positions.

(*ix*) **Suspension of futures trading for a specified period**—This measure is resorted to either by the Presidents or the Governing bodies of recognised associations or by the Commission when an emergency arises in the market. Such a temporary suspension of trading either provides the required time to the authorities to study the market situation, ascertain the causes of emergency and to evolve suitable regulatory measures to deal with the situation without allowing the market to move either way during the period of suspension or helps cooling down of tempers of those frantically engaged in large scale trading.

(*x*) **Closing out of the outstanding contracts**—This may be resorted to only under certain extra-ordinary situations such as a poor harvest, sudden international developments having a bearing on trading in the commodity when orderly trading in a running contract becomes impossible. In such situations, the outstanding contracts are closed out, either at the prevailing rate or at some appropriate rate determined by the authorities depending on the circumstances of the case.

ANNEXURE XIII

PROFORMA OF RETURN

Name of the Exchange/Association ——————————————————————

Full name of the Trader/Operator ——————————————————————

Full business address ——————————————————————

Commodity ——————————————————————

Date on ——————————————————————

Name of the Member through whom traded ——————————————————————

ANNEXURE XIII—*contd.*

Delivery		Previous open contracts or position		Today's trading		Open contracts or position at the close of the day			
						Total*		Classification of open position	
Month	Year	Long	Short	Bought	Sold	Long	Short	Speculative	Hedging@

*This indicates the outstanding position at the end of the day including the previous open contracts or position.

In the U.S.A. every trader who holds or controls **open contracts** in any one future of a commodity in excess of the specified quantity is required to submit the return on the above lines directly to the Commodity Futures Trading Commission. A separate report to be submitted for each commodity.

@**Hedging** : In the Commodity Exchange Act, bonafide hedging is defined as follows :—

Bonafide hedging transaction shall mean sales of any commodity for future delivery on or subject to the rules of any Board of Trade to the extent that such sales are offset in quantity by the ownership or purchase of the same cash commodity or conversely purchase of any commodity for future delivery on or subject to the rules of any Board of Trade to the extent that such purchases are offset by sales of the same cash commodity. There shall be included in the amount of any commodity which may be hedged by any transfer :—

(*A*) The amount of such commodity such person is raising or in good faith intends or expects to raise within the next 12 months, on land (in the United States or its Territories) which such person owns;

(*B*) An amount of such commodity the sale of which for future delivery would be a reasonable hedge against the products or by-product of such commodity owned or purchased by such person, or the purchase of which for future delivery would be a reasonable hedge against the sale of any product or by-product of such commodity by such person;

(*C*) An amount of such commodity the purchase of which for future delivery shall not exceed such person's unfilled anticipated requirements for processing or manufacturing during a specified operating period not in excess of one year; provided that such purchase is made and liquidated in an orderly manner and in accordance with the sound commercial practice in conformity with such regulations as Secretary of Agriculture may prescribe.

(*ii*) Trading limits imposed under the Act to curb excessive speculation does not apply to hedging operations.

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ANNEXURE XIV

LIST OF COMMODITIES IN WHICH NTSD CONTRACTS ARE BANNED OR NOT PERMITTED
(as on 31-3-1980)

A—Commodities in which non-transferable specific delivery contracts are prohibited, in exercise of the powers conferred under section 18(3) of the FC (R) Act.

Sl. No.	Commodity	Region
1	2	3
	Foodgrains and Pulses	
1	Wheat	Entire Country
2	Gram	-do-
3	Jowar	-do-
4	Bajra	-do-
5	Maize	-do-
6	Ragi	-do-

ANNEXURE XIV—*contd.*

1	2	3
7	Small Millets (Kodan, Kutki, Kodra, Korra, Varagu, Sawan, Rala, Kakun, Samai, Vari and Banti)	Entire country
8	Tur (Arhar)	-do-
9	Urad (Mash)	-do-
10	Mung	-do-
11	Moth	-do-
12	Masur	-do-
13	Kulthi	-do-
14	Peas	-do-
15	Lakh (Khesari)	-do-
16	Barley	-do-
17	Guar	-do-
18	Rice or Paddy	-do-
19	Arhar Chuni	-do-
20	Mung Chuni	-do-
21	Tur Dal (Arhar Dal)	-do-
22	Urad Dal (Mash Dal)	-do-
23	Mung Dal	-do-
24	Gram Dal	-do-
Oilseeds, Oils and Oilcakes		
25	Mustardseed	-do-
26	Rapeseed or Toria	-do-
27	Taramiraseed	-do-
28	Mowraseed (Mahuaseed)[1]	-do-
29	Mustardseed Oil[2]	-do-
30	Rapeseed Oil[2]	-do-
31	Taramiraseed Oil[2] (including Sohan Oil and Jamba Oil)	-do-
32	Linseed	-do-
33	Linseed Oil[2]	-do-
34	Castorseed	-do-
35	Cottonseed Oil[2]	-do-
36	Vanaspati, a Vegetable oil[4] product	-do-
37	Mowraseed Oil[1] (Mahuaseed oil)	-do-
38	Neemseed[1]	-do-
39	Neem Oil[1]	-do-
40	Karanja[1]	-do-
41	Karanja Oil[1]	-do-

ANNEXURE XIV—*contd.*

1	2	3
42	Kusumseed[1]	Entire Country
43	Kusum Oil[1]	-do-
44	Sal seed[1]	-do-
45	Sal oil[1]	-do-
46	Khakan Seed[1]	-do-
47	Khakan Oil[1]	-do-
48	Kokum Seed[1]	-do-
49	Kokum Oil[1]	-do-
50	Nahor seed[1]	-do-
51	Nahor Oil[1]	-do-
52	Undi Seed[1]	-do-
53	Undi Oil[1]	-do-
54	Rice Bran[1]	-do-
55	Rice Bran Oil[1]	-do-
56	Watermelon Seed[1]	-do-
57	Watermelon Oil[1]	-do-
58	Tobacco Seed[1]	-do-
59	Tobacco Seed Oil[1]	-do-
60	Sunflower Seed[1]	-do-
61	Sunflower Oil[1]	-do-
62	Niger Seed[1]	-do-
63	Niger Oil[1]	-do-
64	Castor Oil[1]	-do-
65	Sesamum Oilcake	-do-
66	Mustardseed Oilcake	-do-
67	Rapeseed Oilcake	-do-
68	Taramiraseed Oilcake	-do-
69	Cottonseed Oilcake[5]	-do
70	Linseed Oilcake[6]	-do-
71	Cellery seed[7]	-do-

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ANNEXURE XIV — *contd.*

1	2	3
	Fibres	
72	Art Silk Yarn[8] imported into India	Entire country
	Spices	
73	Aniseed	-do-
74	Methi	-do-
75	Coriandersseed	-do-
	Metals	
76	Gold	-do-
77	Silver	-do-
78	Silver Coins	-do-
	Others	
79	Chara or Berseem (including Charseed or Berseemseed)	-do-
80	Gram Husk[1] (Gram Chilks)	-do-

1. NTSD Contracts which are performed wholly by actual tendering of goods and payment of full price therefor, or under which actual tendering of goods becomes impossible or unlawful owning to circumstances beyond the control of the contracting parties, have been exempted.

2. NTSD Contracts which are not regulated by an association are exempted.

3. NTSD Contracts entered into by (i) cottonseed crusher for the sale of cottonseed oil produced by crushing cottonseed in his own mills, and (ii) by a manufacturer of vanaspati for the purchase of cottonseed oil required by him for the manufacture of Vanaspati in his own factory, are exempted.

4. NTSD Contracts entered into by the Central Government or a State Government or on behalf of the Central or State Government by any person or body of persons duly appointed in that behalf by that Government, are exempted.

5. NTSD Contracts entered into by (i) a cottonseed crusher for the sale of cottonseed oilcake, and (ii) an exporter of cottonseed oilcake for the purchase of cottonseed oilcake for the purpose of export out of India, are exempted.

6. NTSD Contracts entered into by (i) a linseed crusher for the sale of linseed expeller cake, (ii) a person exporting linseed extraction cake out of India for the purchase of linseed extraction cake for purposes of export outside India and (iii) a solvent extraction unit for the purpose of linseed expeller cake or the sale of linseed extraction cake, are exempted.

7. NTSD Contracts entered into by a person exporting celleryseed out of India for the purchase of celleryseed for purpose of export outside India, are exempted.

8. NTSD Contracts entered into by (i) the State Trading Corporation of India Ltd., (ii) M/s. Rayex (India) Pvt. Ltd., Bombay, and (iii) Association of Man Made Fibre Industry, Bombay, for sale of art silk yarn imported into India, are exempted.

B—Commodities in respect of which section 15 is applied to non-transferable specific delivery contracts in exercise of the powers conferred under section 18(3) of the FC(R) Act and trading not permitted.

Sr. No	Commodity	Region
1	2	3
	Oilseeds and Oils	
1	Groundnut[9]	Entire Country
2	Groundnut oil[10]	Do.
3	Kardiseed	Do.
4	Kardiseed oil	Do.
5	Sesamum (Til or Jinjili)	Do.
6	Sesamum Oil	Do.
7	Copra	Do.
8	Coconut Oil	Do.
9	Cottonseed[11]	Do.
	Fibres and Manufactures	
10	Kapas[12]	Within the limits of States of Punjab, Haryana, Rajasthan, Uttar Pradesh and the Union Territories of Delhi and Chandigarh.
11	Gur[13]	Entire Country

9. NTSD Contracts entered into by (i) a farmer for the sale of groundnut whole produced by him (ii) the Food Corporation of India, New Delhi or any person or agency duly authorised for the purchase or sale of groundnut-in-shell and groundnut kernels, are exempted.

10. NTSD Contracts entered into by the Central Government or a State Government or by any person duly appointed in that behalf by them, are exempted.

11. NTSD Contracts entered into by (*i*) a ginner of kapas for the sale of cottonseed obtained by him by ginning the kapas in his ginning factory, (*ii*) a dealer in kapas for the sale of Cottonseed obtained by him by getting his kapas ginned, and (*iii*) a cottonseed crusher for the purchase of cottonseed for crushing in his own mill, are exempted.

12. NTSD Contracts within the States of Punjab, Haryana, Rajasthan and Uttar Pradesh and the Union Territories of Delhi and Chandigarh for the purchase of kapas by (*i*) a ginner for ginning in his own factory and (*ii*) a manufacturer of yarn for ginning and utilising the lint obtained therefrom for manufacturing yarn in his own mill, are exempted.

13. Section 15 shall apply only if NTSD Contracts are regulated or controlled by an association.

ANNEXURE XV

AMENDMENTS PROPOSED BY THE COMMISSION IN OCTOBER 1978 TO THE FORWARD CONTRACTS (REGULATION) ACT, 1952

Section 2(a) : As at present

" 'association' means any body of individuals, whether incorporated or not, constituted for the purpose of regulating and controlling the business of the sale or purchase of any goods;"

As proposed to be amended

" 'association' means **an individual or** body of individuals **having the object of** regulating and controlling the business of the sale or purchase of any goods;"

Section 2(f) : As at present

" 'non-transferable specific delivery contract' means a specific delivery contract, the rights or liabilities under which or under any delivery order, railway receipt, bill of lading, warehouse receipt or any other document of title relating thereto are not transferable ;"

As proposed to be amended

" 'non-transferable specific delivery contract' means a specific delivery contract, the rights or liabilities under which or under any delivery order, railway receipt, bill of lading, warehouse receipt or any other document of title relating thereto are not transferable ;"

Provided that where any such contract is performed either wholly or in part :—

(1) by tendering of the documents of title to the goods covered by the contract by any party thereto (not being a commission agent or a bank) who has acquired ownership of the said documents by purchase, exchange or otherwise, to any other person (including a commission agent but not including a bank) ; or

(2) by the realisation of any sum of money, being the difference between the contract rate and the settlement rate or clearing rate or the rate of any offsetting contracts ; or

(3) by any other means whatsoever and as a result of which the actual tendering of the goods covered by the contract or the payment of the full price therefor is dispensed with, then, such contract shall not be deemed to be a non-transferable specific delivery contract.

Explanation : For the purposes of this clause

(i) "bank" includes any banking company as defined in the Banking Regulation Act, 1949, a co-operative bank as defined in the Reserve Bank of India Act, 1934, the State Bank of India and any of its subsidiaries and any corresponding new bank constituted under section 3 of the Banking Companies (Acquisition and Transfer of Undertakings) Act, 1970;-

(ii) "commission agent" means a person who, in the ordinary course of business, makes contract for the sale or purchase of goods for others for a remuneration (whether known as commission or otherwise) which is determined in the contract itself or determinable from the terms of the contract, in either case, only with reference to the quantity of goods or to the price therefor as stipulated in the contract."

Section 2(i) : As at present

" 'ready delivery contract' means a contract which provides for the delivery of goods and the payment of a price therefor, either immediately or within such period not exceeding eleven days after the date of the contract and subject to such conditions as the Central Government may, by notification in the Official Gazette, specify in respect of any goods, the period under such contract not being capable of extension by the mutual consent of the parties thereto or otherwise; ——————————————

——————————————

and as a result of which the actual tendering of the goods covered by the contract or the payment of the full price therefor is dispensed with, then, such contract shall not be deemed to be a ready delivery contract."

As proposed to be amended

" 'ready delivery contract' means a contract which provides for the **actual** delivery of goods within such period not exceeding eleven days after the date of the contract and the payment of a price therefor **fixed at the time of entering into the contract and** subject to such conditions as the Central Government may, by notification in the Official Gazette, specify in respect of any goods, the period **of delivery** under such contract not being capable of extension by the mutual consent of the parties thereto or otherwise;——————————————

——————————————

and as a result of which the actual tendering of the goods covered by the actual contract or the payment of the **value of the goods at the price therefor fixed at the time of entering into the contract** is dispensed with, then, such contract shall not be deemed to be a ready delivery contract".

Section 2(jj) : As at present

" 'registered association' means an association to which for the time being a certificate of registration has been granted by the Commission under section 14B;"

As proposed to be amended

" 'registered association' means an association to which for the time being a certificate of registration has been granted by the Commission under section 14B **in respect of goods or classes of goods and the type or types of forward contracts specified in the certificates of registration;"**

Section 4 B ; As at present

New provision.

As proposed to be amended

"4B. Power of search and seizure

(1) Notwithstanding anything contained in section 22A of this Act or in any other law in force, the Commission may authorise any of its officers not below the rank of Senior Research Assistant to enter and search any place which, he has reason to believe, is being used for the purpose of entering into, making or performing whether wholly or in part any forward contract in contravention of any of the provisions of this Act and or options in goods, or where he has reasons to believe that books of account or other documents pertaining to such contracts or options in goods are being kept, and to seize from such place and/or any person found present there any books of account and/or documents which he suspects to contain material about such contracts or options in goods.

(2) The authorised officer may requisition the services of any Police officers and/or any other officers of the Commission to assist him for all or any of the purposes specified in sub-section (1) and it shall be the duty of every such officer to comply with such requisition.

(3) The provisions of the Code of Criminal Procedure 1973 relating to searches shall, as far as may be, apply to searches under this section subject to the modification that sub-section (5) of section 165 of the said Code shall have effect as if for the word "Magistrate" wherever it occurs, the words the "Forward Markets Commission" were substituted.

(4) If any person wilfully obstructs the authorised officer in the exercise of the powers conferred upon him by or under this section, he shall be punishable with imprisonment which may extend to seven years and with a fine not less than five thousand rupees : provided that in the absence of special and adequate reasons to the contrary to be mentioned in the judgement of the court, the imprisonment shall be not less than one year and the fine shall be not less than five thousand rupees."

Section 4C : As at present

New provision.

As proposed to be amended :

"4C. No act or proceeding of the Commission shall be deemed to be invalid by reason merely of any vacancy or dedefect in the Constitution of the Commission for the time being."

Section 12B(1) : As at present

"If, in the interest of trade or in the public interest, the Commission considers it necessary to suspend a member from his membership of any recognised association or to prohibit such members from entering into any forward contract for the sale or purchase in his own name or through another member of a recognised association of any goods or class of goods, then, notwithstanding anything contained in any law for the time being in force or in the rules or bye-laws of a recognised association, the Commission may, after giving an opportunity to the member concerned of being heard, by order suspend his membership of any association or prohibit him from entering into any such contract."

As proposed to be amended :

"If, in the interest of trade or in the public interest, the Commission considers it necessary to impose a fine on a member or to suspend a member from his membership of any recognised association or to prohibit such a member from entering into any forward contract for the sale or purchase in his own name or through another member of a recognised association of any goods or class of goods, then, notwithstanding anything contained in any law for the time being in force or in the rules or bye-laws of a recognised association, after giving an opportunity to the member concerned of being heard, the Commission may by order impose a fine not exceeding Rs. 25,000 or suspend his membership of any association or prohibit him from entering into any such contract."

Section 14B : As at present

"On receipt of an application under section 14A, the Commission, after making such enquiry as it considers necessary in this behalf, may by order in writing grant a certificate of registration or refuse to grant it :

Provided that before refusing to grant such certificate, the association shall be given an opportunity of being heard in the matter."

As proposed to be amended

"(1) On receipt of an application under section 14A, the Commission, after making such enquiry as it considers necessary in this behalf, may by order in writing grant a certificate of registration or refuse to grant it :

Provided that before refusing to grant such certificate, the association shall be given an opportunity of being heard in the matter.

(2) The certificate of registration granted shall be in such form as may be prescribed and subject to such conditions as may be specified including the type or types of forward contracts which may be traded in by the association and the goods or the classes of goods in which such contracts may be traded in."

Section 14C and 14D : As at present

The existing section 14C of the principal Act shall be renumbered as 14D and in place of section 14C, a new provision as section 14C has been proposed as follows :—

As proposed to be amended

"14C. If the Commission is of opinion that any registration granted to an association under the provisions of this Act, in the interest of the trade or in the public interest be withdrawn, the Commission may, after giving a reasonable opportunity to the association to be heard in the matter, withdraw, by order, the registration granted to the said association :

Provided that no such withdrawal shall affect the validity of any contract entered into or made before the date of the order, and the Commission may make such provisions as it deems fit in the order of withdrawal or in any subsequent order similarly issued for the due performance of any contract outstanding on that date."

Section 18(1) : As at present

"Nothing contained in Chapter III or Chapter IV shall apply to non-transferable specific delivery contracts for the sale or purchase of any goods :

Provided that no person shall organise or assist in organising or be a member of any association in any area to which the provisions of section 15 have been made applicable (other than a recognised association) or any which provides facilities for the performance of any non-transferable specific delivery contract by any party thereto without having to make or to receive actual delivery to or from the other party to the contract or to or from any other party named in the contract."

As proposed to be amended

"Nothing contained in Chapter III or Chapter IV shall apply to non-transferable specific delivery contracts for the sale or purchase of any goods :

Provided that no person shall organise or assist in organising or be a member of any association other than a recognised association in any area to which the provisions of section 15 have been made applicable and of any association in any area to which the provisions of section 17 have been made applicable which provides facilities for the performance of any non-transferable specific delivery contract by any party thereto without having to make or to receive actual delivery to or from the other party to the contract or to or from any other party named in the contract."

Section 20(i) and (ii) : As at present

"(i) for a first offence, with imprisonment which may extend to one year, or with a fine of not less than one thousand rupees, or with both;

(ii) for a second or subsequent offence under clause (d), or under clause (e) (other than an offence in respect of a contravention of the provisions of sub-section (4) of section (15), with imprisonment which may extend to one year and also with fine; provided that in the absence of special and adequate reasons to the contrary to be mentioned in the judgement of the court, the imprisonment shall be not less than one month and the fine shall be not less than one thousand rupees."

As proposed to be amended

"(i) for a first offence, with imprisonment which may extend to three years and also with a fine of not less than three thousand rupees : **provided that in respect of offences under clause(d) or under clause (e) other than an offence in respect of a contravention of the provisions of sub-section (3A) and (4) of section 15, in the absence of special and adequate reasons to the contrary to be mentioned in the judgement of the court, the imprisonment shall be not less than six months and the fine shall be not less than three thousand rupees.**

(ii) for a second or subsequent offence, under clause (d), or under clause (e) other than an offence in respect of a contravention of the provisions of sub-section (3A) and (4) of section 15 with imprisonment which may extend to seven years and also with a fine : provided that in the absence of special and adequate reasons to the contrary to be mentioned in the judgement of the court, the imprisonment shall be not less than one year and the fine shall be not less than five thousand rupees."

Section 21(a) : As at present

"owns or keeps a place other than that of a recognised association, which is used for the purpose of entering into or making or performing, whether wholly or in part, any forward contracts in contravention of any of the provisions of this Act and knowingly permits such place to be used for such purposes, or"

As proposed to be amended

"owns or keeps a place which is used for the purpose of entering into or making or performing, whether wholly or in part, any forward contracts **or options in goods** in contravention of any of the provisions of this Act and knowingly permits such place to be used for such purposes, or"

Section 21(c) : As at present

"manages, controls or assists in keeping any place other than that of a recognised association, which is used for the purpose of entering into or making or performing, whether wholly or in part, any forward contracts in contravention of any of the provisions of this Act or at which such forward contracts are recorded or adjusted, or rights or liabilities arising out of such forward contracts are adjusted, regulated or enforced in any manner whatsoever, or"

As proposed to be amended

"manages, controls or assists in keeping any place which is used for the purpose of entering into or making or performing, whether wholly or in part, any forward contracts **or options in goods** in contravention of any of the provisions of this Act or at which such forward contracts **or options in goods** are recorded or adjusted, or rights or liabilities arising out of such forward contracts **or options in goods** are adjusted, regulated or enforced in any manner whatsoever, or".

Section 21(f) : As at present

"joins, gathers, or assists in gathering at any place, other than the place of business specified in the bye-laws of a recognised association, any person or persons for making bids or offers or for entering into or making or performing whether wholly or in part, any forward contracts in contravention of any of the provisions of this Act, or"

As proposed to be amended

"joins, gathers, or assists in gathering at any place or any person or persons for making bids or offers or for entering into or making or performing, whether wholly or in part, any forward contracts or options in goods in contravention of any of the provisions of this Act, or"

Section 21(i) and (ii) : As at present

"(i) for a first offence, with imprisonment which may extend to two years, or with a fine of not less than one thousand rupees, or with both;

(ii) for a second or subsequent offence, with imprisonment which may extend to two years and also with fine : provided that in the absence of special and adequate reasons to the contrary to be mentioned in the judgement of the court, the imprisonment shall be not less than one month and the fine shall be not less than one thousand rupees".

As proposed to be amended

"(i) for first offence, with imprisonment which may extend to three years and also with a fine of not less than three thousand rupees : provided that in the absence of special and adequate reasons to the contrary to be mentioned in the judgement of the court, the imprisonment shall be not less than six months and the fine shall be not less than three thousand rupees;

(ii) for a second or subsequent offence, with imprisonment which may extend to seven years and also with a fine : provided that in the absence of special and adequate reasons to the contrary to be mentioned in the judgement of the court, the imprisonment shall be not less than one year and the fine shall be not less than five thousand rupees."

Section 21(bb) and (bc) : As at present

New provision.

As proposed to be amended

"(bb) organises or assists in organising an association, other than a recognised association, to which a certificate of registration has not been granted under this Act; or

(bc) organises, or assists in organising, manages, controls or assists in keeping a registered association or is a member of a registered association which is carrying on business relating to forward contracts in violation of conditions in the certificate of registration granted to it under this Act; or"

Section 21A and 21B : As at present

The existing section 21A, be renumbered as 21B and a new provision as 21A has been proposed as follows :—

As proposed to be amended

"21A. If any person contravenes any of the provisions of this Act or of any rule, direction or order made thereunder for the contravention of which no penalty is expressly provided, he shall on conviction be punishable :—

(*i*) for a first offence with imprisonment which may extend to three years and also with a fine of not less than three thousand rupees: provided that in the absence of special and adequate reasons to the contrary to be mentioned in the judgement of the court, the imprisonment shall be not less than six months and the fine shall be not less than three thousand rupees;

(*ii*) for a second or subsequent offence, with imprisonment which may extend to seven years and also with a fine : provided that in the absence of special and adequate reasons to the contrary to be mentioned in the judgement of the court, the imprisonment shall be not less than one year and the fine shall be not less than five thousand rupees."

Section 21C : As at present

New provision.

As proposed to be amended :

After renumbering section 21A of the principal Act as 21B, the following section shall be inserted thereafter namely :—

"21C. Notwithstanding anything contained in section 29 of the Code of Criminal Procedure, 1973 (2 of 1974), it shall be lawful for any Chief Judicial Magistrate or any Magistrate of the First Class to pass any sentence authorised by this Act in excess of his powers under the said Code."

Section 22B(1) : As at present

"Where any books of account or other documents are seized from any place and there are entries therein making reference to quantity, quotations, rates, months of delivery, receipt or payment of differences or sale or purchase of goods or option in goods, such books of account or other documents shall be admitted in evidence without witnesses having to appear to prove the same; and such entries shall be prima facie evidence of the matters, transactions and accounts purported to be therein recorded."

As proposed to be amended :

"Where any books of account or other documents are seized from any place or persons in persuance of the warrant issued under section 22A(1) above or in persuance of section 165 of the Criminal Procedure Code read with section 23 below and there are entries therein making reference to quantity, quotations, rates, months of delivery, receipt or payment of differences or sale or purchase of goods or option in goods, such books of account or other documents shall be admitted in evidence without witnesses having to appear to prove the same; and such entries shall be prima facie evidence of the matters, transactions and accounts purported to be therein recorded."

Section 23A : As at present

New provision.

As proposed to be amended

"23A. Nothing contained in section 360 of the Code of Criminal Procedure, 1973 or in the Probation of Offenders Act, 1958, shall apply to a person convicted of an offence under this Act unless the person is under eighteen years of age."

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